S. HRG. 100-197

CASH MANAGEMENT IMPROVEMENT ACT OF 1987

HEARING

BEFORE THE

SUBCOMMITTEE ON GOVERNMENT EFFICIENCY, FEDERALISM, AND THE DISTRICT OF COLUMBIA

OF THE

COMMITTEE ON GOVERNMENTAL AFFAIRS UNITED STATES SENATE

ONE HUNDREDTH CONGRESS

FIRST SESSION

ON

S. 1381

TO IMPROVE CASH MANAGEMENT BY EXECUTIVE AGENCIES, AND FOR OTHER PURPOSES

JULY 22, 1987

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CASH MANAGEMENT IMPROVEMENTS ACT OF 1987

WEDNESDAY, JULY 22, 1987

U.S. SENATE,
SUBCOMMITTEE ON GOVERNMENT EFFICIENCY,
FEDERALISM, AND THE DISTRICT OF COLUMBIA,
COMMITTEE ON GOVERNMENTAL AFFAIRS,
Washington, DC.

The Subcommittee met, pursuant to notice, at 10:30 a.m., in room SD-342, Dirksen Senate Office Building, Hon. Jim Sasser (chairman of the Subcommittee) presiding.

Present: Senators Sasser, Roth, and Heinz.

OPENING STATEMENT OF SENATOR SASSER

Senator SASSER. The Subcommittee will come to order.

I want to say good morning to our distinguished Ranking Minority Member, Senator Roth, the former chairman of the full Committee. We are delighted to have Senator Roth here with us this morning. Also, I want to say good morning to the witnesses and to interested parties.

This morning the Subcommittee on Government Efficiency, Federalism, and the District of Columbia is pleased to consider S. 1381, the Cash Management Improvement Act of 1987. I cosponsored this bill last month, with my distinguished colleague from Delaware, Senator Roth, to implement the recommendations of the Joint Federal/State Cash Management Reform Task Force.

Overall, the Federal Government now spends more than $1 trillion a year. That is an absolutely staggering sum, and in the area of Federal aid to State and local Governments, the Federal Government disburses $110 billion annually through 435 separate Federal aid programs.

This aid goes to 50 State Governments and to more than 39,000 local Governments across the United States, and therein lies the problem. For without the reforms proposed by this Federal cash management bill, there is little uniformity in the way in which Federal funds are disbursed to State and local Governments.

Over the years we have had unnecessary friction between the Federal and State Governments over the timing of cash transfers to the States to carry out Federal programs. Federal agencies felt that their State counterparts were requesting drawdowns of Federal funds too far in advance of need, resulting in undue loss of interest earnings to the Federal Treasury.

But the States, too, can point to examples where they have had to advance funds to carry out Federal programs, such as highway construction, and lost interest while waiting for reimbursement from the Federal Treasury.

Now, studies by the Joint Financial Management Improvement program in 1981 and 1982 showed that there was some justification for complaints on the part of both the Federal Government and local and State Governments. Making the situation worse was that each Federal agency and its State counterpart tended to use different cash transfer procedures than other departments and other agencies. There was no uniformity, in other words.

A State/Federal Task Force was formed in 1983 to come up with solutions to the problem, and as a result of the Task Force's work over a 4-year period, it recommended that each State decide and agree with the Department of the Treasury on a single cash transfer formula for all the Federal programs carried out by that State.

The State/Federal Task Force oversaw pilot programs in four States which showed that cash management provisions did work. The theme is cooperation instead of competition.

The Congressional Budget Office has estimated that on the whole, the Federal Government loses some $56 million a year in interest—that is serious money by anybody's standards—that could be earned on Federal funds that are sent to State and local Governments in advance of their being disbursed by these State and local Governments.

In this case, the State and local Governments benefit by the float of Federal aid. At the same time, some State and local Governments have had to disburse their own funds to cover other Federal aid programs, and this costs these local and State Governments about $10 million a year in foregone interest on cash investment.

So the sum total is that passage of this bill benefits Federal, State and local Government, but most importantly it benefits the American taxpayer, perhaps to the tune of $50 million a year.

For that reason I am delighted to hear that both Federal and State officials are enthusiastic about the passage of this legislation. The same provision was reported favorably by the full Governmental Affairs Committee last year as part of S. 2230, but too late in the session to receive full consideration by the Senate.

We hope now to get cash management reform written into law so that we can begin to realize the fruits of the work that the State/Federal Task Force has done.

Let me defer now to my distinguished colleague, Senator Roth, for any statement or comment that he might wish to make.

Senator Roth?

OPENING STATEMENT OF SENATOR ROTH

Senator ROTH. Thank you, Mr. Chairman.

First, I want to express my great appreciation to you for holding the hearing today and, of course, for cosponsoring the legislation. As you pointed out, we did report out similar legislation last year, but unfortunately it did not get considered at that time.

I want to say a little about why this bill authorizes the exchange of interest between the Federal Government and the States. The

interest exchange provision in the bill provides an incentive for the timely exchange of funds. If this were a perfect world, this provision would not be necessary, but unfortunately, experience has shown that States do not always get funds from the Federal Government when they need them, and not all States have historically waited until they need funds to draw them down.

Clearly, we must develop cash transfer policies that are fair, uniform, predictable as well as enforceable. Currently the Intergovernmental Cooperation Act, which this bill amends, falls short of providing for uniformity and predictability.

While some States have felt that the act prohibits the Federal Government from collecting interest from the State, in truth it prohibits only in certain instances. The interest prohibition only applies to grant money pending its disbursement for program purposes. Therefore, the interest prohibition does not apply to some funds, like R&D grants, that are specifically excluded from the definition of grant.

These exemptions to the interest prohibition have led to confusion, not just to the State, but to the agencies that are attempting to require the States to pay interest under a variety of programs.

S. 1381, the Cash Management Improvement Act of 1987, which I introduced with Senator Sasser, makes it clear when interest should be paid by either the Federal Government or the State. It also provides for a simplified approach for calculating interest, rather than the multiple ways currently being advanced by the different Federal agencies. Pilot tests conducted by States demonstrated that interest would be calculated without significant changes or increases in staff.

It is also important to point out that States need not choose a funding option that calls for the interest exchange. Options are available that would not require the exchange of interest and the U.S. Treasury will work with States to ensure a mutually agreeable option for the drawing down of funds.

I think it is noteworthy that both the National Association of State Auditors, Comptrollers and Treasurers and the National Association of State Budget Officers have called for this bill. These groups have had members on the State/Federal Cash Management Reform Task Force since its inception and they endorse the content of the bill, which closely follows the legislation developed by the Task Force.

I am pleased that with this legislation the Congressional Budget Office has taken a look at it for cost savings and they have concluded, based on past Treasury information, that this should save the Federal Government about $50 million a year. It is a timely piece of legislation, both in concept and in result. I am pleased to see the action being taken here.

Thank you, Mr. Chairman.

Senator SASSER. Well, thank you very much, Senator Roth, for your statement and for your continued interest in this whole problem.

Our first witness this morning will be the Honorable Gerald Murphy, Fiscal Assistant Secretary from the Department of the Treasury.

Mr. Murphy, if you would, please come forward. We welcome you here this morning, Mr. Murphy, and we look forward to your statement.

For the benefit of the record, would you be good enough to identify your colleague who is accompanying you there?

TESTIMONY OF GERALD MURPHY, FISCAL ASSISTANT SECRETARY, U.S. DEPARTMENT OF THE TREASURY, ACCOMPANIED BY DR. RUSSELL D. MORRIS, ASSISTANT COMMISSIONER FOR FEDERAL FINANCE, FINANCIAL MANAGEMENT SERVICE

Mr. MURPHY. Yes. Thank you, Mr. Chairman. Accompanying me this morning is Dr. Russell Morris, who is Assistant Commissioner for Federal Finance of the Financial Management Service of Treasury.

Mr. Chairman, it is a pleasure to be here today to discuss ways to improve the equity of money transfers between the Federal Government and the States through the vehicle of exchanges of interest payments. S. 1381, the Cash Management Improvement Act of 1987, is the first substantial legislative action taken by the 100th Congress to establish a means for this action.

On June 15, 1987, the administration transmitted a legislative proposal to Congress which addresses many of the same issues. The need for such a legislative solution has received wide support from State Governments and all segments of the public financial community.

The Financial Management Service of Treasury is the organization which has worked on this project for a considerable period of time, and which would be the responsible organization for implementing such legislation. Dr. Morris, who is with me today, is also the Co-Chairman of the State/Federal Cash Management Reform Task Force.

Over the past 4 years, Treasury and the administration have fully supported the initiative that is called the State/Federal Equity Program. In its role as lead agency, the Financial Management Service has provided a co-chairman and staff support for the Task Force; conducted four pilot programs to test the reciprocal interest concept; provided speakers for numerous conferences and meetings; and produced periodic news letters for mailing to 1,000 State and Federal recipients.

During this time, the effort has been actively supported by the Office of Management and Budget and Treasury. The administration has submitted legislative proposals to the Congress in 1986 and 1987. Both Treasury and the Office of Management and Budget cooperated with the National Association of State Auditors, Comptrollers and Treasurers last fall to conduct a seminar to acquaint State and Federal representatives with the new funding concept. The seminar was attended by over 275 individuals representing 44 States and all of the major Federal agencies.

This project is a natural responsibility for the Financial Management Service which manages the collection, investment and payment of nearly $2 trillion each year. They use a wide variety of sophisticated technology to manage Federal funds, oversee the Government's central accounting and reporting system, and provide

many services which touch the lives of virtually all Americans, from Social Security recipients to taxpayers receiving income tax refunds.

Interestingly, the Financial Management Service earns $10 for every $1 that is appropriated to it.

Senator SASSER. Would you repeat that, Mr. Murphy?

Mr. MURPHY. Yes, sir.

Senator SASSER. Earns how much?

Mr. MURPHY. The Financial Management Service, through its efforts to improve cash management, credit management and financial management in Government, actually saves the taxpayers $10 for every $1 appropriated for those functions.

Senator SASSER. If we appropriate enough money for that service, it would wipe out the deficit at that rate. Go ahead.

Mr. MURPHY. I would like to make a few brief comments on S. 1381 and then respond to any questions that you and Senator Roth might have.

We support the thrust of S. 1381. However, there are a few differences between this bill and the administration's bill which I would like to address. First, section 3(a) of S. 1381 is apparently designed to provide the Secretary of the Treasury with broad authority over all Federal disbursements. The administration's bill establishes regulations which cover only transfers of funds between the Federal Government and the States.

We believe that the broad authority contemplated by this section needs to be discussed further with other Federal agencies and the Office of Management and Budget to determine the full impact of such a change before we take a position on it.

Second, the proposed subsection 6503(d) of title 31 provides that if a State disburses its own funds for program purposes in accordance with Federal law, regulation or Federal/State agreement, the State shall be entitled to interest. This seems to entitle the States to interest, whether or not a Federal agency is at fault. The administration's bill proposes that States be entitled to interest if the State disburses its own funds at a time and for purposes for which the Federal Government is obligated to pay but has not provided funds.

The other significant concern we have is with proposed subsection 6503(l). This provision implies that the Government will pay States for additional administrative costs for interest transactions. We believe the administrative cost of the improvements contained in this bill should be treated as a general overhead cost of Government like any other administrative cost.

Section 4(b)(1) of S. 1381 also seeks to improve the collection and deposit of Government receipts through national lockbox systems. The Financial Management Service of the Department of the Treasury has successfully operated and managed a national lockbox system since 1983. The system currently services 281 programs for 60 agencies. Through June 30, 1987, $15.3 billion had been collected during the fiscal year with a projected increase to $20 billion by September 30, 1987. This will result in an estimated savings of $23.6 million to the taxpayers for fiscal year 1987.

While the Department of the Treasury is in complete accord with the purposes of this section, we believe that Treasury has sufficient

authorities to achieve the purposes under the Deficit Reduction Act of 1984 and earlier legislation.

While we strongly favor the administration's legislative proposal, Treasury supports the overall intent of S. 1381 and looks forward to working with you to accomplish the purposes of this bill.

That concludes my remarks, Mr. Chairman, and I will be happy to respond to questions.

Senator SASSER. Well, Mr. Murphy, let me just ask you about what appears to be a point of departure between the bill, S. 1381 as introduced and some statements that you have made this morning.

You indicate that section 3(a), entitled disbursements objectives, seems to give the Secretary of the Treasury overly broad authority over all Federal disbursements, not just Federal disbursements to States to carry out Federal programs.

You also indicate that perhaps that needs to be discussed further with other Federal agencies; is that correct?

Mr. MURPHY. Yes, sir, just to determine what the full impact of that provision would be.

Senator SASSER. Right. Well, I would like to point out that identical language was contained in the version of this legislation considered last session by the Governmental Affairs Committee and was reported out by the Governmental Affairs Committee, and I believe that OMB, after the bill was reported, submitted a version of the bill for consideration by the House and Senate, which is almost identical to the one that has been received this past month.

Are you aware of that?

Mr. MURPHY. I am not aware that OMB had submitted a version which is identical to this one.

Basically, I am not rejecting the proposal but I am just not in a position at this point in time to take a position on it.

Senator SASSER. Do you know of any reason why OMB has not formulated a position on section 3(a)?

Mr. MURPHY. No, sir. The language here is quite similar to authority that we were given earlier to impose similar types of charges when agencies do not follow collection and deposit regulations. This appears to be quite similar to that.

One concern we have is that in the collection area, that authority was used primarily not to charge other agencies and transfer a lot of money to Treasury, but to get agencies to perform the collection and deposit function correctly. So it was used as a lever. The authority to impose charges on other agencies as yet has not actually been used.

In this area, we feel that the wording here on the disbursement side may have a little different implication and may result in a far greater number of charges to agencies. So we just want to be sure we understand the impact.

Senator SASSER. All right. Mr. Murphy, I may have additional questions that we would like to submit for the record later, but I would like now to defer to my colleague, Senator Roth, for any questions or comments that he may have.

Senator ROTH. Yes. One question I would like to ask you, Mr. Murphy, is in what ways is the Department of the Treasury prepared to work with a State in order to reach a mutually agreeable option without an interest exchange?

Mr. MURPHY. Senator Roth, we have attempted to offer a variety of mechanisms whereby States can achieve essentially the same overall purpose without the reciprocal interest arrangement, and there are arrangements in place that are options for States to choose from, such as the checks paid letter of credit method and the delay of drawdown letter of credit method.

Senator ROTH. How effective an enforcement tool do you see the interest provision? Do you see it as being used often?

Mr. MURPHY. The interest provision in section 3(a)?

Senator ROTH. Yes.

Mr. MURPHY. I would see that there may be a number of situations where we would be utilizing that provision. I do not have a feeling for any exact numbers.

Senator ROTH. That is all the questions I have. Thank you, Mr. Chairman.

Senator SASSER. Thank you, Senator Roth.

I want to thank you very much, Mr. Murphy, for your attendance here this morning, and I want to express my appreciation to Dr. Morris for accompanying you also and for the assistance he has been as Co-Chairman of the State/Federal Cash Management Reform Task Force, and the time that he has devoted and the attention that he has devoted to this issue.

Gentlemen, thank you both for appearing. Again, Mr. Murphy, we may have one or two additional questions for you which we would submit for the record, and if they are forthcoming, if you would respond in an expeditious manner, we would appreciate it.

Mr. MURPHY. Thank you, Mr. Chairman.

Senator SASSER. Thank you.

Our next witness this morning is Mr. Jeffrey C. Steinhoff. Mr. Steinhoff is the Associate Director of Accounting and Financial Management Division of the United States General Accounting Office, known affectionately around here as the GAO.

Mr. Steinhoff, it is a pleasure to have you here this morning and we look forward to receiving your testimony, and if you would kindly introduce your colleague for the record, we could get started.

TESTIMONY OF JEFFREY C. STEINHOFF, ASSOCIATE DIRECTOR, ACCOUNTING AND FINANCIAL MANAGEMENT DIVISION, U.S. GENERAL ACCOUNTING OFFICE, ACCOMPANIED BY CHRIS MARTIN, SENIOR ACCOUNTANT

Mr. STEINHOFF. With me today is Chris Martin, Senior Accountant with GAO, who has been instrumental in our cash management work.

Mr. Chairman and Senator Roth, we are very pleased to be here today to give our views on the Cash Management Improvement Act of 1987, S. 1381. I have a detailed statement which I would like to submit for the record and will summarize my remarks.[1]

GAO has long called for strengthened Federal cash management and fully supports S. 1381. We see this bill as an important opportunity to continue progress in better managing the Government's

[1] See p. 37.

financial affairs. We also believe it is important in another respect; it is a good example of what can be achieved by a joint cooperative effort of State and Federal representatives working together to solve a longstanding problem.

For many years, intergovernmental financing arrangements have been a source of contention between the Federal Government and the States. The problems, causes and impediments to easy solutions have been well documented.

In short, the Federal Government has been concerned about States drawing down Federal funds sooner than necessary to cover disbursements on Federal programs, and States have complained that they often do not receive Federal funds soon enough and must use their own cash to finance Federal programs.

Both parties recognized that viable solutions, fair to both sides, had to be developed, and with Congressional urging, formed the State/Federal Cash Management Reform Task Force in 1983. The results of 4 years of excellent work by the Task Force, composed of Federal and State financial officials and including representatives of the Office of Management and Budget, are reflected in section 4 of S. 1381.

The bill would establish intergovernmental cash management practices which assure that neither the Federal nor State Governments profit or suffer financially as a result of the transfer of cash. Equity is the key, treating each party in the same fair manner.

The provisions of section 4 are fair to both parties, represent the reasoned judgment of Federal and State Task Force members and will resolve a longstanding point of contention. We supported these concepts last year when they were part of S. 2230, which passed the Senate Governmental Affairs Committee. We continue to fully support these concepts today.

We also support section 3 of S. 1381. The Deficit Reduction Act of 1984 provided additional tools to the Secretary of the Treasury to help assure that Federal agencies follow sound cash management concepts in collecting and depositing Federal funds. The act requires that agencies' collection practices comply with Treasury regulations. In cases where they do not, Treasury may assess an agency for the cost of any losses to the Government.

This authority, however, as you earlier pointed out, does not extend to disbursements which exceed a trillion dollars each year. S. 1381 remedies this problem.

We do offer one technical suggestion. The Subcommittee may wish to specify in section 3 that interest penalties assessed by Treasury should be paid out of appropriations available for agency operations to the extent they can be, and not reduce amounts available to fund programs. We understand that this has been a concern of the States.

Finally, we support section 5 in calling for the improved collection and deposit of Government receipts through lockbox systems. These systems can speed up receipts and eliminate deposit delays.

Mr. Chairman, this concludes my summary remarks. Again, we fully support S. 1381 and stand ready to work with the Subcommittee as it considers the bill. We would be pleased at this time to respond to any questions that you or members of the Subcommittee may have.

Senator SASSER. Thank you, Mr. Steinhoff.

Senator HEINZ. Mr. Chairman, may I make a unanimous consent request?

Senator SASSER. Well, Senator Heinz, you certainly may, and we are pleased to have you here this morning. We welcome you to the Subcommittee, and you may make any request that you wish.

Senator HEINZ. Well, Mr. Chairman, that is an extraordinary offer, but I will constrain myself.

I want to apologize to you, Mr. Chairman, and our witnesses, but the confirmation hearing that we have in the Banking Committee prevented me from being here for the opening of this hearing, and I have a statement I would like to make a part of the record at the appropriate point.

Senator SASSER. It will be included in the record.

[The statement of Senator Heinz follows:]

OPENING STATEMENT OF SENATOR HEINZ

Mr. Chairman, thank you for this opportunity to learn more about the legislation which you and Senator Roth, the distinguished past chairman of the committee, have developed. At present we have not even-handedly dealt with the issue of cash management.

Under the multitude of Federal programs which transfer funds from the Treasury to the States, there has not been a fair way to account for Federal cash. The Grace Commission found that some States were drawing down Federal funds prematurely. Meanwhile, the Joint Financial Management Improvement Program found that some other States were forced to draw down their own cash, when Federal funds were not promptly forthcoming for the program in question.

The legislation before the subcommittee would authorize a system of interest transfer. The concept of the legislation has been that whoever has the benefit of cash, be it a Federal agency or a State government, pay interest on that cash. By requiring interest payments, either from the State to the U.S. Treasury for funds drawn prematurely, or from the Federal Government to the States for funds delayed, the legislation seeks to prod Federal and State agencies to manage Federal moneys in a sound and sensible fashion. Passing the buck has been radically redefined to "passing the interest!" It's a whole new kind of fiscal responsibility—as opposed to shirking responsibility, it means assuming responsibility.

These are certainly worthy goals. In my own State of Pennsylvania, a pilot test of the annual grant award process for HHS programs is currently being conducted. The findings of that pilot test, and the hearing record being developed today, will be of great help to the Congress in developing an appropriate response.

I look forward to reviewing the testimony of today's outstanding panel of witnesses. Thank you, Mr. Chairman, for this opportunity, and for your initiative.

Senator HEINZ. Mr. Chairman, I thank you.

Senator SASSER. Thank you, Senator Heinz.

Well, Mr. Steinhoff, I have no questions for you at this time.

Mr. Steinhoff of the General Accounting Office has just completed his testimony, Senator Heinz. Do you have any questions?

Senator HEINZ. No, Mr. Chairman, I do not.

Senator SASSER. All right.

Mr. Steinhoff, thank you for appearing here this morning. We appreciate the General Accounting Office's work in this whole field, and I think that the efforts of GAO in calling for strengthened Federal cash management over a period of some time has

been most helpful in creating an atmosphere in which a bill such as S. 1381 could be brought forth and, hopefully, passed in this session of the Congress.

Thank you very much.

Mr. STEINHOFF. Thank you, Mr. Chairman.

Senator SASSER. Next, a group of witnesses will appear as a panel. They are the Honorable Frank Greathouse, the Director of the Division of State Audit, and also Assistant Comptroller of the State of Tennessee, and Mr. Greathouse, we welcome you here today; and Mr. Edward J. Mazur, Co-Chairman of the Joint State/Federal Cash Management Reform Task Force, who when not performing that task is the Comptroller of the Commonwealth of Virginia. We welcome you, Mr. Mazur. Also, we have Mr. Arnold Schuler, the Deputy Controller, State of California, and Ms. Beverly Balakhovsy, Chief Accountant of the State of Wisconsin.

It is a pleasure to have all of you here this morning, and I want to extend a particular warm welcome to my great good friend, Frank Greathouse, who has performed so admirably for so many years in his position for the State of Tennessee. He is indeed a dedicated public servant in the truest sense of the word.

Frank, we welcome you here today and we will begin with any statement or comment that you wish to make.

TESTIMONY OF FRANK L. GREATHOUSE, DIRECTOR, DIVISION OF STATE AUDIT, ASSISTANT COMPTROLLER, STATE OF TENNESSEE; [1] EDWARD J. MAZUR, CO-CHAIRMAN, JOINT STATE/FEDERAL CASH MANAGEMENT REFORM TASK FORCE, COMPTROLLER, COMMONWEALTH OF VIRGINIA; [2] F. ARNOLD SCHULER, DEPUTY CONTROLLER, STATE OF CALIFORNIA; [3] AND BEVERLY BALAKHOVSKY, CHIEF ACCOUNTANT, STATE OF WISCONSIN [4]

Mr. GREATHOUSE. Thank you, Mr. Chairman. It is a pleasure to be here before you. I will not bore you reading the paper I have presented for your consideration. I do think that this morning after hearing Treasury's testimony, we have solved the national deficit problem.

I really think if we appropriate $100 billion to that particular program, that we will indeed—if it yields 10 to 1—solve the annual budget deficit. I suggest that maybe we consider that.

Senator SASSER. Well, we have another Federal agency that takes the same approach. The IRS takes the view, I think, that every additional dollar that is appropriated for them over a certain amount produces something like $1,000. So if we would just appropriate enough money for the IRS, we would be running surpluses shortly.

Mr. GREATHOUSE. That is right, and I think we ought to try some of those just to see if they work, just for one year.

In any case, my purpose in being here this morning is to point out the historical importance of Congress' considering and passing this legislation, which would be another step or a link in intergov-

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[1] See p. 46 for Mr. Greathouse's prepared statement.
[2] See p. 68 for Mr. Mazur's prepared statement.
[3] See p. 75 for Mr. Schuler's prepared statement.
[4] See p. 81 for Mr. Balakhovsky's prepared statement.

ernmental cooperation. I think it is high time that we, who are responsible for Government in these United States, consider Government at the three levels as being a cooperative enterprise to serve the constituency.

We should stop thinking in terms of Federal dollars, State dollars, and local dollars. These are public monies that need to be carefully spent economically and efficiently for the benefit of those taxpayers whom we all serve.

Beginning with the great turnover or turn back to the States and to local Governments of large amounts of Federal dollars through Federal assistance programs in the 1960's, an adversarial relationship almost immediately sprang up between the three levels of Government. Through the efforts of senior fiscal managers of State Government and the Federal Government, there has been a 20-year effort to stop that adversarial relationship and to bring about fiscal cooperation.

I list in the paper presented to you several very successful ongoing efforts that point out we can work together at the three levels of Government to do what is necessary to serve the constituency.

It seems to me that this bill, the Cash Management Improvement Act of 1987, is just another step in the right direction. I would point out that I appeared before your Committee on sunset some time earlier, again on access to Federal tax data by the State auditors, and again on the Single Audit Act. All of these were steps in an effort to improve the fiscal management of government.

Several other such efforts are under consideration today. We in State and local Government really owe a debt of appreciation to the Federal Government for several things that have happened. Through the passage of revenue-sharing legislation, you brought about better accounting, auditing, and financial reporting at the State and local Government level.

That was closely followed by the Single Audit Act, which has brought about conservation of audit resources at the Federal, State and local levels. We now obtain through one audit and the use of scarce audit resources an audit that is usable at all levels of Government, at a significant savings to the taxpayer, and that provides better auditing, better disclosure, and better financial reporting.

This act is in the same tenor as those acts. We need to thank the Federal Government for bringing about legislation that has helped us so much. All of a sudden the States are ahead of the Federal Government. Twenty years ago, each State had its own reporting system; it was on the the cash basis and did not provide adequate disclosure. Nobody knew what was going on.

Local government in the mid-1970's began to have bonds going into default. Governments were in huge deficit positions and in violation of their own laws. All of that has been reversed because you forced upon us at the Federal level certain financial reforms that are beneficial to us. We thank you for that.

We encourage you to go forward. I think we now need to flip the coin. I believe that the Federal Government should practice what it has preached for so long. If it is good for us, perhaps it is good for you, too.

We know that the General Accounting Office, through its leader, Comptroller General Bowsher, is pushing several initiatives, of

which cash management is only one. Other reforms need to be put in place that will make bills like the one we are considering today unnecessary in the long run.

One reform is to create a Federal Chief Financial Officer who will have authority to act entity-wide. We need to control what I describe as the multi-headed Medusa we in State Government have to deal with when we deal with the Federal Government. We never know who the Federal Government is because one day it is this person, and the next day it is another. Maybe the Chief Financial Officer would remedy that situation.

The Federal budget continues to be in disarray. There is no such thing as a Federal accounting system, based on generally accepted accounting principles. Audited financial statements are unheard of. All of these are things that you have required of State Governments. We have met your requirements.

Almost every State now either is keeping its records according to GAAP or generally accepted accounting principles. Almost all are audited. We meet the disclosure requirements of the bond market in New York. We meet the Federal requirements for a single audit.

Once again, this Committee needs to move toward some reform at the Federal level. We will support you in that. As President-elect of the Government Finance Officers Association, I will seek their support for financial reform in the Federal Government.

As auditors who have to audit these people, not as cash management technicians, we think this bill within itself is a necessary reform. We know what the bill does is right. We know that it needs to be done. It brings about equity. There are no gainers, there are no losers. The taxpayer will gain in these circumstances.

With that, I will make myself available for any questions you might have.

Senator SASSER. Thank you very much, Frank. We will come back for questions later.

We will move on now to Mr. Mazur.

Mr. MAZUR. Sir, I would first of all like to say informally that those of us in a leadership position in the financial affairs of our State look to this fine Tennessean as a national treasure, a person on whose leadership we rely a great deal.

Senator SASSER. Well, we in Tennessee agree with you on that, Mr. Mazur.

Mr. MAZUR. My name is Edward Mazur and I am Comptroller of the Commonwealth of Virginia, past President of the National Association of State Comptrollers, and Co-Chairman since 1983 of the State/Federal Cash Management Reform Task Force.

I am here today on behalf of the National Association of State Auditors, Comptrollers and Treasurers to speak in support of the intergovernmental financing provisions found in Senate Bill 1381.

In addition to my appearance before you today, I have submitted written testimony that explains more completely the role of the Cash Management Reform Task Force in formulating the intergovernmental financing provisions. I have also attached to that written testimony three technical amendments which we believe add clarity to certain aspects of the bill and which we would be pleased to discuss with you and members of your staff following today's testimony.

I am here today, Mr. Chairman, principally because of a Senate colloquy held by nine Senators in 1983. This colloquy led to a request from the Senate to OMB that appropriate Federal agencies work with State representatives to develop improved policies guiding the transfer of cash between the Federal Government and the States and that equity be clearly a part of those policies.

Since 1983, 12 senior State and Federal officials, including at one time two elected State treasurers have labored as the State/Federal Cash Management Reform Task Force to accomplish the following: First, the initial drafting of proposed policies that would ensure the timely movement of monies to the States in support of Federal programs; second, the rigorous evaluation of these policies, some 17 in number, through a year-long pilot testing in California, Indiana, Wisconsin and Virginia; third, the resolving of several equity issues, principally relating to the timeliness of grant awards, the handling of questioned costs, and the way in which we can ensure uniformity in the interpretation of Federal requirements; fourth the formulation of a formal memorandum of understanding in 1985 which recommended the legislation that you now have before you, and which also put forth specific recommendations as to the supporting administrative requirements that would be appropriate to the legislation.

Senator, as noted in my written testimony, an important element in the Memorandum of Understanding, although not in the bill, concerned the endorsement of the testing of the Annual Grant Award procedures by the Department of Health and Human Services, and this testing is now going on in 7 States. I recommend to this Subcommittee that you consider the results of this testing when it is available, because of the natural association between the Annual Grant Award initiative and the equity provisions that are found in S. 1381.

The time I have before you today is certainly limited in terms of reviewing, in detail, the various intergovernmental financing provisions, but I do want to take a minute, Mr. Chairman, to give you some assurances relative to the interest exchange provisions found in the bill. They are necessary to help both State and Federal officials monitor their respective performances under the funds transfer provisions of the bill, and it is the funds transfer provisions that are the focal point of this bill, not the interest exchange provisions. Interest exchange is a facilitator for sound transfer practices.

If the States pay the Federal Government interest, actually what they will be doing is simply accumulating that interest from the time the funds pass to the States until the time checks clear the banks of the States. Accordingly, utilization of other revenues to make such interest payments should, under most all normal circumstances, not be involved.

It is important to note relative to section 6503(d), which was mentioned by Mr. Murphy this morning, that interest owed to the Federal Government or to the States will be calculated based solely on who uses the funds, not based on fault.

For example—and this is a rather basic one—if a Federal payment to a State is delayed because a Federal employee in a particular department is sick, there is no difference in the impact from the case where the illness of a State employee delays a State's re-

quest to have funds transferred. Fault is not an equitable criteria. Only the use of money is, and that is what S. 1381 provides.

In addition, as it relates to Section 6503(l), it is critical that the Secretary of the Treasury be granted the authority to consider costs incurred by States when calculating interest due. The States believe that these costs should not be handled as though they were part of some grant or aid program, as is the case with most all other Federal monies.

The unique objectives of this legislation we believe require the Secretary of the Treasury be given the authority to consider such costs when formulating the Federal/State agreement which will be formulated between the Secretary of the Treasury and each State on a separate basis, and therefore we do believe this is a special authority that is appropriate to the Secretary of the Treasury.

In closing my remarks this morning, Mr. Chairman, let me quickly cite for you what I believe will be the most significant benefits to both the States and the Federal Government that would be derived by the timely enactment of the intergovernmental financing provisions: First, that there will be essential fairness in the way in which the States and Federal Government conduct their financial affairs; second, the premature drawdowns of funds by States, as has been noted by the Grace Commission Report, will cease and therefore Federal funds will be available for longer period of time to the Federal Government to use for other purposes before these monies are committed to the States; third, States will no longer be required, as noted by JFMIP studies in 1982, to use their own tax revenues in support of Federally assisted programs while awaiting the receipt of Federal funds; and fourth, senior State officials, such as comptrollers and treasurers, will share important new opportunities with their U.S. Treasury Department counterparts to monitor and refine the manner in which the billions of dollars of Federal monies from the Federal Government to the States.

This legislation will bring the attention of all of these parties to a common point of focus. Thus, Mr. Chairman, this legislation I believe closes the loop between the expressions of interest and direction given by the Senate in 1983 and today's hearing on proposed legislation that has already been proven in the field.

Thus, we hope that this Subcommittee, and ultimately the full Senate, will give speedy and favorable consideration to the intergovernmental financing provisions found in S. 1381.

It is a pleasure to be with you today.

Senator SASSER. Mr. Mazur, thank you for your very excellent statement.

We will turn now to Mr. Schuler, the Deputy Controller of the State of California. Do you have anything you wish to add, Mr. Schuler?

Mr. SCHULER. Good morning, Mr. Chairman. I am Arnold Schuler, Deputy Controller for the State of California. Since 1983 I have been one of six members on this Cash Reform Task Force. As you know, this Task Force drafted the proposal which forms the basis for this bill.

I am very pleased to offer my comments this morning on three areas. One, I want to talk a bit about Ed Mazur's testimony, I want

to talk about the reimbursement for administration costs, and then finally I would like to comment briefly on the Treasury testimony and the Administration bill.

First of all, I would certainly like to thank you, Senator Sasser and Senator Roth and this Committee for promoting and overseeing the work of the Task Force. Without that, I know that we would not be at this position right now with this bill.

In terms of Ed Mazur's testimony, I think that it is very important that the amendments that we have included in the written testimony, if you find fit, be amended into the bill. We want to make sure that no interest is paid to the States that comes out of program funds. We have one amendment that does take care of that issue. We think that is important.

Also, we have an amendment that talks about that this bill that covers all Federal/State cash transfer programs, including construction grant programs. We want to make it clear in the bill that no Federal programs are excluded. We think that is critical.

In terms of administrative costs, administration costs for the interest exchange program, we have been talking about this since 1983. We think it is very important the States are reimbursed for this. The original Memorandum of Understanding (MOU) instructed the pilot States to determine the methods for providing administrative and start-up costs attributable to the specific cash management practices being implemented. There was specific language along those lines.

We knew that there was going to be an additional cost to the State and that it was essential when we did these pilots that those were identified so that when we got started with this program, the States could receive some help from the Federal Government in that area.

The payment for administration costs continues the make-whole concept, where neither the Federal Government nor the State should benefit or suffer from the use of the other's funds. So we want to make sure we do get paid for those.

In the pilot tests that were conducted where these costs were collected, we found certain things. First, we found that the interest costs can be tracked and they can be computed. We also found that the States will need very well structured systems to track these Federal and State funds that are used in Federal assistance programs.

If they do not have such systems, they are going to have to build them and there is going to be a cost associated with that. We also found that it is going to be very expensive for the States to track exceptions, because usually these exceptions reside outside the given systems of the State.

The Treasury has asserted many times that it will be very simple to both compute interest and to track costs. We think the pilots have proven that in many cases there will be some simple things that we can do, but in most cases the exceptions will be costly and difficult to track.

The pilots determined that in one State the costs were $7,500 to conduct the pilot while in another they were $43,000. These were additional costs to the State. They did not represent all of the pro-

grams. They did clearly demonstrate that once these programs start, that the States will incur new costs.

Because all the burden of record keeping is on the States, we believe that the States should be reimbursed for the costs. This is consistent with the MOU policy which states that neither Federal or State Governments should benefit or suffer financially as a result of the transfer of cash in support of a Federal assistance program.

So the payment for these costs would be similar to the States being paid for other administrative costs when we are providing services to the Federal Government; for instance, like AFDC would get paid for administrative costs. So I urge your Committee to retain paragraph [l] of S. 1381, and possibly even strengthen that section in order to make sure that the States do get paid for these costs.

In terms of the Treasury testimony, until this morning I do not think that the State members, at least the ones that are here, were aware of the Federal Government's opposition to the basic make-whole concept which is the foundation of the MOU in your bill. We are really quite surprised that they would oppose this, because both Treasury and OMB were parties to the MOU and actually parties to the Task Force proposed bill.

We are very concerned that the OMB bill is looking at fault prior to instituting the application of interest provisions. As Ed Mazur mentioned, the intent by both the Federal and State was to arrive at a smooth flow of cash to fund essential Federal assistance programs. There should be no winners or losers and we should be striving for effectiveness in our programs.

Also, we are concerned about the OMB testimony that the payment for the cost of administering the interest exchange program should be treated as a general overhead cost. The problem with this is that States will get no new money in order to fund this effort, and I think from the beginning we talked about the need for that.

Additionally, the bill sent to Capitol Hill on June 15th by the Administration, which we do not think has been introduced yet, has a number of conflicts with the agreements reached by the Federal and State Task Force members. This bill is similar to an OMB bill sent to Congress last year which was not introduced prior to adjournment.

Last year we sent a letter—the State members—to OMB Deputy Director Joseph Wright, which outlined why we oppose the Administration bill, and we want to furnish that for the record today if we can.[1]

I think I can speak for all the Task Force members that this bill that is being proposed by the Administration does not represent signed agreements reached between the State and Federal members, and as a result, it is impossible for State members to support the OMB measure.

I think it is really disheartening that at this late date the State members are concerned about the Treasury and OMB good faith in

[1] See p. 84.

the negotiation process. This process was originally instituted by this Committee during the 98th Congress when you requested OMB to work with the States to arrive at an equitable cash management process which was fair to both the States and Federal Government.

I think we arrived at that agreement through negotiation and now we find ourselves with the Administration coming forward with a bill that is in direct conflict with that.

I would be pleased to answer any questions.

Senator SASSER. Thank you very much, Mr. Schuler. We will come back for questions.

Ms. Balakhovsky, we would be delighted to hear from you now.

Ms. BALAKHOVSKY. Thank you, Mr. Chairman.

I am Beverly Balakhovsky, Chief Accountant of the State of Wisconsin. I want to thank you for giving me the opportunity to address you this morning on S. 1381.

As a member of the Task Force, I want to endorse the comments made by Mr. Mazur and Mr. Schuler. The concepts embodied in S. 1381 were carefully negotiated and crafted by the State and Federal members of the Task Force to ensure that there are no winners and no losers in the exchange of funds between the Federal Government and the States.

The Administration bill deviates from this carefully negotiated and crafted language to the point where it jeopardizes the no winner and no losers make-whole concept. Your bill, however, provides the framework to achieve this equity for both levels of Government, and the immediate beneficiaries of this equity are the taxpayers.

Interest provides a quantitative basis for identifying problems and inefficiencies at both the State and Federal levels. The Task Force and the pilots have demonstrated that resolving problems and improving efficiency is not only possible, but that it may be one of the most effective ways to achieve cash management improvements in the Federal and State Governments.

During the pilots it became clear that there were inequities to the States that would be better resolved by attempting to change the factors that caused the problems than by calculating the interest. An example is the quarterly grant award process for State-administered Federal programs. The quarterly process causes a number of difficulties for States. It interrupts the State's access to needed and allowable Federal cash and forces the State to use its own funds.

This temporary use of State monies reduces the State's investment opportunities on its own monies, thereby in effect causing the State to subsidize the Federal programs in ways that were never intended by Congress. The quarterly award process results in an excessive amount of unnecessary paperwork at both the State and Federal level and does not improve the accountability at either level.

In response to the issues raised by the quarterly process, the Task Force agreed that HHS should test an annual award process in seven States. It is important to note that this annual process does not allow the States to draw the money at one time, but in fact requires the State to time the draw to meet actual expenditures as they are made.

The purposes of the pilot as described in the memorandum of understanding are to reduce the paperwork requirements and administrative costs associated with the quarterly awards; to minimize the periodic interruption in State access to needed and allowable Federal cash; to achieve equity in the State/Federal cash flow; and to improve the level of accountability.

The pilot tests are being conducted during Federal fiscal year 1987 and are occurring in seven States—Wisconsin, Tennessee, Indiana, Louisiana, Nebraska, Pennsylvania, and Virginia.

I would especially like to thank you, Mr. Chairman, for your assistance in initiating the Annual Grant Award pilot. OMB expressed opposition to this project. However, through the assistance of you and your staff, the objections were overcome and the project was allowed to begin this year.

Even though the pilots are not yet completed, there are some preliminary results that I would like to share with you. The Annual Grant Award process has significantly reduced administrative and paperwork burdens at both the Federal and State level. It has reduced the number of times the State's access to Federal cash is interrupted, thereby saving the State of Wisconsin over $250,000 in potentially lost investment earnings on State funds which would have been used temporarily for Federal programs.

It has demonstrated that equity can be achieved in a cooperative State/Federal venture. There are significant benefits at both the Federal and State levels, such as increased efficiency, improved controls and systems, more effective use of staff resources, and improved cash management. The Annual Grant Award process is simpler, easier and provides better accountability at both levels of Government.

Based on these preliminary results, I would recommend that the seven pilots continue the Annual Grant Award process as they select and implement the cash management improvements as embodied in S. 1381. The Department of Health and Human Services will be issuing a report on the results of the Annual Grant Award in early 1988. I would respectfully encourage the subcommittee to closely examine this report in light of the benefits that I believe will result for both the Federal and State Governments.

Should the report demonstrate that the Annual Grant Award program is a positive step toward equitable cash management, the State members of the Task Force may once again request the Subcommittee's help in extending the program to all of the States as they individually select and implement the concepts of improved cash management as embodied in S. 1381.

In closing, Mr. Chairman, I want to again thank you for giving me this opportunity to comment on the importance of S. 1381 and the Annual Grant Award as being critical and effective ways to assure equity and to effect the necessary cash management improvements at the State and Federal level, which will ultimately benefit the taxpayer and more efficient Government at all levels.

Thank you.

Senator SASSER. Thank you very much, Ms. Balakhovsky.

Let me just ask you a question, Mr. Mazur, or perhaps you, Mr. Schuler—whoever might wish to comment. OMB's proposal diverges from some of the provisions in S. 1381, as I think one or per-

haps both of you noted. And one provision with which OMB differs is that States would be entitled to interest without fault by the Federal Government.

Now, this whole subject was considered by your Task Force; was it not?

Mr. SCHULER. I can answer that, Mr. Chairman. It was the basic issue, something that we have talked about from the very beginning. It was the Federal Government, through OMB and Treasury, that pushed the idea of interest. They wanted this interest to flow both ways. That is why at this point in time we are just amazed that we are hearing this from OMB.

What it sounds like is that they want this to be a one-way street where if the States use Federal funds, the States always pay interest, and only if the States can find Federal fault, would the Federal Government pay the States interest. We find this incredible.

Senator SASSER. Well now, there was a 1985 memorandum of understanding which incorporated a draft bill, if I am not mistaken, and in that memorandum this whole business of interest between the Federal Government and the State Governments was included. It made no mention of fault being a condition precedent, as I understand it, for the Federal Government's obligation to pay interest; is that not correct?

Mr. SCHULER. That is correct, Mr. Chairman. In fact, the memorandum of 1983 between the parties, which OMB and Treasury were parties to, as well as the memorandum of 1985, which appended that memorandum, all went along with this same issue of no fault.

Senator SASSER. And did not both Treasury and OMB sign that memorandum or indicate that it had their approval?

Mr. SCHULER. Yes, they did, Mr. Chairman.

Senator SASSER. So now we are hearing from OMB that they differ with the legislation in that the Federal Government should pay interest only if there is fault.

Mr. SCHULER. That is right, Mr. Chairman.

Senator SASSER. And the burden would be on the State Government to prove fault.

Mr. SCHULER. That is right, Mr. Chairman.

Senator SASSER. Mr. Mazur, do you wish to comment?

Mr. MAZUR. May I add, Mr. Chairman, that section (b) on page 4 includes the words that a State shall minimize the time elapsing between the transfer of funds from the United States Treasury and the issuance or redemption of checks, warrants or payments by other means for program purposes.

That is very powerful language and a lot of thought went into that and it is complementary to the words that appear over in section (d) on page 5. And there is also wording in section (a) which indicates to the Federal agencies, the Executive agencies, that they should schedule the transfer of funds to minimize the time elapsed.

That is why I said in my remarks a few minutes ago that the cornerstone of this legislation is not the interest, but it is the provision of an effective funds transfer mechanism. There is a sense of discipline, from a policy point of view, that is embodied in this legislation that says to both State people and to Federal people, transact your business in the shortest amount of time, have it flow

smoothly, and have it flow in a knowledgeable way; not as it has in the past.

We believe and have confidence, based on the pilots, that the Federal people can make adjustments. We know through the pilot testing that states can make adjustments in our behavior on a day-to-day basis. Therefore, if we start getting into nuances on a program-by-program, transaction-by-transaction level in terms of who, on this normal day-to-day basis, was at fault, as it affects the timing of funds, we are going to throw the concept of this legislation off base.

If you look at (d), it explains it quite clearly just in the first three sentences—the State disperses its own funds for program purposes. In other words, good work is done at the bequest of the Federal Government in accordance with Federal law or regulations or Federal/State agreement. And the Federal/State agreement is another powerful control the legislation gives to the Secretary of the Treasury because it will be the Secretary that signs that agreement or enters into that agreement through his officers with the various States.

So there are very adequate protections to prevent anything untoward from going on vis-a-vis interest exchange, but yet the legislation recognizes that if states use their own money, they should be allowed to consider it when calculating interest, the same as if it goes the other way. We think it is an honest and a good approach to the problem.

Senator SASSER. Well, I agree with you Mr. Mazur. Now, Mr. Schuler referred to a letter of December 12, 1986 that was written to Joe Wright of OMB. Mr. Wright is the Deputy Director and he appears before this Committee and other Committees rather frequently.

You wrote that letter, did you not, Mr. Mazur?

Mr. MAZUR. I did.

Senator SASSER. And you outlined in that letter a number of provisions, including this provision about the payment of interest, which is the basic premise of the whole legislation. Did OMB ever respond to your letter of December 12, 1986 to your knowledge?

Mr. MAZUR. Not in writing. We did receive assurances from the OMB representative to the Task Force that they were actively considering a letter. I know that he personally worked very hard within OMB as they considered the 1985 MOU to incorporate and consider my concerns.

It is apparent, absent any other direct information or any written response from Director Wright, that as the Administration went through its final considerations of the MOU there were just simply people in OMB, perhaps not on the intergovernmental side of the fence but perhaps the budget side, who felt some concerns and their concerns became embodied in what the Administration finally came out with.

I certainly want to acknowledge with appreciation that the President and OMB officials have given time and attention to this initiative, as have the States, and I think it is unfortunate that differences have appeared.

I think the overall concept, hopefully, is still adhered to by OMB, but we do hope that you will go with your legislation, Senator, be-

cause a lot of these points were negotiated over many, many months. The balancing of legitimate interests was constantly being weighed during the course of these Task Force meetings.

No one was a pure winner. The States were not a pure winner. The Federal Government was not a pure winner. It was just a good compromise. Compromise means that both sides gave. Your bill, I think, takes all of that into consideration, and we would ask, respectfully, if you would hold to your position, because we think that is the one that will really do the best job possible.

Senator SASSER. Well, I can assure you that we are going to do our very best to maintain our position.

Let me ask you this, Mr. Greathouse, just by way of illustration of what we are trying to drive at here. Could you give us some idea where the State of Tennessee, for example, stands in terms of outstanding expenses for Federal programs that you might be awaiting reimbursement for? Have you got a ball-park figure for that, based on your experience?

Mr. GREATHOUSE. I was asked that question a couple of weeks ago and I could not give a clear answer because we have not attempted to measure it very accurately. We do know that we are not able to draw down money in the Department of Transportation as rapidly as we expend it. Some of that is due to the deficiencies in our own accounting system, which we are currently remedying. We will put in a new system almost momentarily. That will alleviate it some.

We hope that that will bring about a more equitable area there. To give you an estimate of how much it is, it would amount to several million dollars in monies over a period of a year that we could not draw down quite as rapidly as we should.

Senator SASSER. Do you have any figure in mind how much interest the State of Tennessee, for example, might gain under this legislation?

Mr. GREATHOUSE. Well, I am not sure that we have ever looked at it to see whether we gain or lose. We have looked at it to see what is fair. We have been a gainer in several programs; we have been a loser in other programs.

The last time we measured that, of course, was four or five years ago with the JFMIP study, and we were a very definite loser in that incident. That has been remedied somewhat. We were maybe as much as $10 million at that time a loser, purely because we were delinquent in education and transportation. We remedied as much of that as we can.

Maybe we are a loser to the extent, of $3 or $4 million at the current time, but that is a ballpark estimate.

Ms. BALAKHOVSKY. I could provide information from the State of Wisconsin. We have been tracking the details of what we would have drawn if we could have, and on an average daily balance there is currently between $10 and $20 million of State funds being used for Federal programs, and this is a decrease from previous years. It was higher in previous years. Participating in the cash management and annual grant award pilots is directly responsible for this decrease. That will give you some idea of the magnitude for Wisconsin.

Senator SASSER. Well, that would be helpful.

Mr. MAZUR. In 1982, if you weighed the balance on any given day, Virginia was using more of its own money in support of Federal programs than we were getting in. That was principally because of the way in which we recovered monies from the Federal highway program.

All of that has changed. Virginia was one of the pilot test locations, and now we have eliminated both premature and late drawdowns. We draw our money down as we need it, but not prematurely, and so I would say that with certain minimum exceptions we are getting the money as we need it and we are having it there a couple of days before we actually disburse it, and that is what is comprehended in the bill.

Senator SASSER. Is the highway program the principal culprit with regard to the States having to advance their own funds?

Mr. MAZUR. It is the single biggest program that the JFMIP studies of eight States showed in 1982, yes.

Ms. BALAKHOVSKY. The entitlement programs are another large issue of that type.

Senator SASSER. Any one particular type of program?

Ms. BALAKHOVSKY. The AFDC, Medicaid, foster care, child support—those are the programs which usually end up forcing States to use their own monies.

Senator SASSER. Now, the Committee Counsel has suggested that I ask this question of you, Mr. Schuler, for the record. You mentioned the cost to States of implementing the interest exchange program. Do you know how much, for instance, California's cost would be?

Mr. SCHULER. I am going to hedge a bit here. We think that in order to run this program properly we are going to need about five people on a central basis, so we are talking probably about $250,000 right there, plus any systems work that we have to do. So we could be talking up to $500,000 a year for this program. Now, I would like to mention that we think we are going to owe the Federal Government interest on a regular basis, so we would be deducting that cost from any interest that is owed, so there would not be a payment out of the Treasury to us for that cost. It would just be a net type of item.

Senator SASSER. You would be deducting from the interest that the Federal Government would owe?

Mr. SCHULER. No. We would owe the Federal Government. We think that the State of California on a regular basis will owe the Federal Government interest, and the reason for that is, in order for us to make our payments, we have to have the Federal money first. So we are willing to pay interest for the period of time that we hold that until we redeem our checks or warrants.

So on a regular basis we will probably have to pay the Federal Government money. From that we would deduct these administrative costs.

Senator SASSER. Then this question follows. Why should the State be fully reimbursed for its costs? Under subsection (1) it says your costs would be, in terms of the statute, "considered" by the Treasury.

Now, might this include splitting the cost with the Federal Government? The question poses itself, why should the State be fully reimbursed for their cost of implementing the program?

Mr. SCHULER. Okay. I think that one thing that the States really have given on in this whole program is the fact that we are paying full interest on the float. We are going all the way to the point where we redeem checks and warrants and we are going to pay that money over to the Federal Government. We agreed to do that. We think that is a major consideration that we have gone for in this.

As a result of that, we think we should be reimbursed for these administrative costs. We think that that is a fair exchange. So that is one reason that I think we should be fully reimbursed.

Senator SASSER. Does anybody wish to amplify on Mr. Schuler's answer? Mr. Greathouse.

Mr. GREATHOUSE. No, not on his answer.

Mr. MAZUR. Well, I think that Virginia's outcome would be comparable, though sized down, given the size of our State versus California. We will probably end up owing interest to the Federal Government; not the other way around.

We now bill the Highway Administration on a daily basis, which is probably the most aggressive schedule of any State in the country. Our administrative costs might end up being in the neighborhood of one person and some support costs, not a great amount of money. The authority given to the Secretary of the Treasury to consider administrative costs when developing the Federal/State agreement is something that we consider to be very important.

The Treasury Department, really, will be the leading agency on this program, and we would like to see that Secretary have all that he or she needs to do the job.

Ms. BALAKHOVSKY. In Wisconsin, the cost to implement this will be relatively minimal. We will not be running the same scale as California and we will not be paying interest back to the Federal Government in the same scale as California, because we do not require the funds on hand in advance of writing our checks. So for Wisconsin, I think, we will be a net winner.

But what we are talking about is all of the States, and I do not know the picture for the rest of the States. My guess is it is somewhere between Wisconsin and California in terms of the systems that they have available and whether they are, in fact, a net winner or a net loser.

Senator SASSER. Thank you.

Mr. Greathouse, did you have a comment to make?

Mr. GREATHOUSE. Yes, sir. In preparation for coming here I had some discussions with our former State Treasurer Harlan Matthews, current State Treasurer Steve Adams, and with David Manning, who is our current Finance Commissioner in an effort to determine what would be the real effect upon the State for this kind of legislation. Not looking at gainers or losers, but to see what we could do.

Tennessee is very innovative in how it invests its idle funds. Anything that we can do that helps us further forecast monies that are going to be available for investment earns us more money. We

have gotten very sophisticated, as have most States, in how we manage our idle funds.

This is a yield to the taxpayer, again, not looking at the cost. We already have the cost of doing that now. I do not know how we would determine an added cost. The cost is whatever is related to that portion of the funds lying there that represents Federal funds. The whole idea of this, I think, is that this type of legislation would help us to better forecast by the leveling of the flow of moneys back and forth.

You get a better handle on it, and therefore you put it into your computer software systems that help you better to forecast to get more money out that you can invest and earn it, and you are earning that from those banks that need the money and are willing to pay you for the use of the State's idle funds.

Therefore, it is a benefit to the taxpayer, all taxpayers. And then if there is a distribution back to the Federal Government, so be it. That is the part of the software program that makes the distribution anyway.

That is the attitude that we are taking in the State on it. Hopefully we can get into the same thing in our Department of Transportation that he now has the privilege of because it was a pilot State. I wish now that Tennessee had been the last pilot State rather than the first one, because that concept would not have worked 5 years ago when we were involved in it.

One other comment. This thing that has arisen as to the position of the Office of Management and Budget is really indicative of why this legislation is so necessary. Management and Budget should take out of its name "management," because they do not do a lot of it, frankly. They are a budget-driven organization. Management is a byproduct with them and they only do it when they are forced to, and then they do it very poorly.

Our dealings with them are that if you do not get legislation, you get erratic management. Therefore, legislation is necessary in order that we get the proper reaction to what they are indeed attempting to manage. So we urge that that legislation be put in place.

It had to happen in the Single Audit Act, if you recall. They had attachment P to circular A-102, and they could not manage it. They never managed it. They could not get it going. It is going perfectly now. You put it in legislation and it is working very nicely. I think GAO will report that to you when they finish their current ongoing examination.

That is it.

Senator SASSER. Well, that is a point well made.

Do you wish to amplify on that, Mr. Schuler?

Mr. SCHULER. Mr. Chairman, I do not want to prolong this, but I would like to comment once more about this administrative cost and why we think it is important, at least in California, to be reimbursed for that.

We think we run a pretty fair investment program in the State. However, in this particular area, this will be an additional cost to the State, and the State was very concerned when this issue was discussed that that would be an additional function that we would have to perform for the Federal Government.

So all along when we have been selling this in the State, trying to get people to approve it, we have always said that it was a part of the agreement that this would be paid for by the Federal Government. That was a part of the sales pitch, and so I think if we were not paid for it, there would be a lot of people in our State that were very disappointed by the fact that they thought it had been agreed to and now it was not any longer.

So I would just like to make that point. It is a fairly substantial cost, but we will be paying to the Federal Government probably about $10 million a year, so when I say it is $500,000, which seems like a lot of money, that would be netted from that figure. So the Fed really would not have to disburse that from the Treasury.

Mr. MAZUR. And all the State members share that concern with California, and feel the same as Arnold is expressing.

Senator SASSER. Well, all right. I want to thank all of our witnesses for appearing here today.

This hearing has been very helpful to the Committee, particularly this last panel, and we intend to drive forward and doubt not in our efforts to get this legislation adopted by the full Senate.

We are going to keep the record open until July 29 for any additional comments or statements that interested parties might wish to make.

Do you wish to make an additional comment, Frank?

Mr. GREATHOUSE. I would like to recognize to you the fact that this gentleman I have been conferring with back here is the Assistant Commissioner for Human Services from the State of Tennessee. He has been an active member of this Task Force and is keeping those of us in Tennessee who are very interested in this matter completely informed and up to date on the matter. His name is Lewis Harris, and I think you met him in the hallway earlier.

Senator SASSER. I did. Mr. Harris, we are pleased to have you here with us today. Thank you for the contributions you have made to this Task Force.

There being nothing further to come before the committee today, the committee will stand in recess.

[Whereupon, at 11:57 a.m., the Subcommittee adjourned subject to the call of the Chair.]

ADDITIONAL MATERIAL SUBMITTED FOR THE RECORD

100TH CONGRESS
1ST SESSION

S. 1381

To improve cash management by executive agencies, and for other purposes.

IN THE SENATE OF THE UNITED STATES

JUNE 17, 1987

Mr. ROTH (for himself and Mr. SASSER) introduced the following bill; which was read twice and referred to the Committee on Governmental Affairs

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A BILL

To improve cash management by executive agencies, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Cash Management Improvement Act of 1987".

PURPOSE

SEC. 2. It is the purpose of this Act to increase the efficiency of efforts to manage cash throughout the Government by providing additional procedures and incentives for cash management.

DISBURSEMENT OBJECTIVES

SEC. 3. (a) Subchapter II of chapter 37 of title 31, United States Code, is amended by adding at the end thereof the following new section:

"§ 3720B. Disbursement of Federal funds

"Each head of an executive agency (other than the Tennessee Valley Authority) shall, under such regulations as the Secretary of the Treasury shall prescribe, provide for the timely disbursement of Federal funds through cash, checks, electronic funds transfer, or any other means identified by the Secretary. The Secretary may collect from any executive agency which does not comply with the preceding sentence a charge in an amount the Secretary determines to be the cost to the general fund of the Treasury caused by such noncompliance. The amounts of the charges paid under this subsection shall be deposited in the Cash Management Improvements Fund established under section 3720(c) of this title.".

(b) The chapter analysis for chapter 37 of such title is amended by inserting after the item relating to section 3720A the following new item:

"3720B. Disbursement of Federal funds.".

(c) The Secretary of the Treasury shall prescribe regulations, including the regulations required under subsection (a) of section 3720B of title 31, United States Code (as added by subsection (a) of this section) to ensure the full implementation of such section 3720B by October 1, 1988.

PAYMENT OF INTEREST

SEC. 4. (a) Section 6501 of title 31, United States Code, is amended—

(1) by redesignating clauses (7), (8), and (9) as clauses (8), (9), and (10), respectively;

(2) by inserting after clause (6) the following new clause:

"(7) 'Secretary' means the Secretary of the Treasury."; and

(3) by striking out clause (9) (as redesignated by clause (1) of this subsection) and inserting in lieu thereof the following:

"(9) 'State' means a State of the United States, the District of Columbia, a territory or possession of the United States, and an agency, instrumentality, or fiscal agent of a State but does not mean a local government of a State.".

(b)(1) Section 6503 of title 31, United States Code, is amended to read as follows:

"§ 6503. Intergovernmental financing

"(a) Consistent with program purposes and with regulations of the Secretary, and by means mutually agreed upon by the Secretary and a State, the head of an executive agency carrying out a program shall schedule the transfer of funds to minimize the time elapsing between transfer of funds

from the United States Treasury and the issuance or redemption of checks, warrants, or payments by other means by a State.

"(b) Consistent with program purposes and with regulations of the Secretary, and by means mutually agreed upon by the Secretary and a State, a State shall minimize the time elapsing between transfer of funds from the United States Treasury and the issuance or redemption of checks, warrants, or payments by other means for program purposes.

"(c)(1) The Secretary shall issue regulations that will require a State to pay interest on funds from the time that funds are deposited to the State's account until the time that funds are paid out in order to redeem checks or warrants or make payments by other means for program purposes. Such interest shall be calculated at a rate equal to the average of the bond equivalent rates of 13-week Treasury bills auctioned during the period for which interest is calculated, as determined by the Secretary.

"(2) Amounts received as payment of interest under this subsection shall be deposited in the Treasury and credited as miscellaneous receipts, except as provided in paragraph (3) of this subsection.

"(3) If interest is paid under paragraph (1) of this subsection on funds paid to a State from a trust fund for which the Secretary of the Treasury is the trustee, or from the Un-

employment Trust Fund, such interest shall be credited to such trust fund.

"(d) If a State disburses its own funds for program purposes in accordance with Federal law, regulation, or Federal-State agreement, the State shall be entitled to interest from the time when the State's funds are paid out to redeem checks or warrants, or make payments by other means, until the Federal funds are deposited to the State's bank account. The Secretary shall pay, out of any money in the Treasury not otherwise appropriated, such amounts as may be necessary for interest owed to a State under this subsection. Such interest shall be calculated, at a rate equal to the average of the bond equivalent rates of 13-week Treasury bills auctioned during the period for which interest is calculated, as determined by the Secretary.

"(e) The budget submitted by the President under section 1105 of this title for a fiscal year shall include a statement specifying, for the most recently completed fiscal year, amounts of interest paid to the Federal Government under subsection (c) of this section and payments of interest to States under subsection (d) of this section.

"(f) If a State receives refunds of grant funds, the State shall return those refunds to the executive agency administering the grant program or apply those funds to reduce the amount of funds owed to the State under such grant pro-

gram. Interest earned on such refunds shall be considered when setting overall interest obligations between the State and the Federal Government as required by this section.

"(g) If the Federal Government makes a payment to a recipient under a Federal program, and a portion of the payment is an amount which the Federal Government is paying to such recipient on behalf of a State, such amount shall be considered to be a transfer of funds between the Federal Government and the State for purposes of this section.

"(h) A State may not be required by a law or regulation of the United States to deposit grant money received by it in a separate bank account. However, a State shall account for grant money made available to the State as United States Government grant money in the accounts of the State. The head of the State agency concerned shall make periodic authenticated reports to the head of the appropriate Federal executive agency on the status and the application of the money, the liabilities and obligations on hand, and other information required by the head of the executive agency. Records related to the grant received by the State shall be made available to the head of the executive agency and the Comptroller General for auditing in accordance with chapter 75 of this title.

"(i) The Secretary shall prescribe the methods of payment of interest between the Federal Government and the

States, including provisions for offsetting amounts owed by the respective parties. Such methods of payment shall provide for comparable treatment in manner, technique, and timing for both the States and the Federal Government.

"(j) The Inspector General of an executive agency, or an officer of an executive agency performing functions similar to an Inspector General, in the case of an agency in which an Inspector General has not been established by law, shall periodically conduct audits of the implementation of this section. Periodic audits of the implementation of this section shall also be conducted by the States within the scope of work performed under chapter 75 of this title.

"(k) Consistent with Federal program purposes and regulations of the Secretary, the head of a Federal executive agency carrying out a program shall execute grant awards on a timely basis to assure the availability of funds to accomplish transfers in compliance with subsection (a) of this section.

"(l) In determining the amount to be paid by a State to the Federal Government under subsection (c) of this section, or to a State by the Federal Government under subsection (d) of this section, the Secretary shall consider costs incurred by the State determining the amount due.".

(2) The item relating to section 6503 in the chapter analysis for chapter 65 of title 31, United States Code, is amended to read as follows:

"6503. Intergovernmental financing.".

(c) The provisions of this section and the amendments made by this section shall apply to all Federal programs and shall supersede the provisions of any Federal law or regulation in effect on the date of enactment of this Act.

(d) The amendments made by this section shall take effect on the date of enactment of this Act, except that the provisions of section 6503 of title 31, United States Code (as added by subsection (b) of this section) which relate to the payment and receipt of interest by the Federal Government and State governments shall take effect two years after the date of enactment of this Act.

IMPROVING THE COLLECTION AND DEPOSIT OF GOVERNMENT RECEIPTS THROUGH NATIONAL LOCKBOX SYSTEMS

SEC. 5. (a) For purposes of this section—

(1) the term "executive agency" has the same meaning as in section 102 of title 31, United States Code;

(2) the term "lockbox system" means a system under which—

(A) persons owing payments to an executive agency transmit such payments to a locked post office box in offices of the United States Postal Service; and

(B) such payments are collected from such box by a financial institution and are credited by

such institution to the account of such agency without any specific action by such agency; and

(3) the term "Secretary" means the Secretary of the Treasury.

(b) The Secretary shall study and make recommendations concerning standards for the establishment of lockbox systems for executive agencies. In conducting such study, the Secretary shall—

(1) consider—

(A) the feasibility of establishing such systems;

(B) the benefits and costs of establishing such systems; and

(C) the needs of each executive agency for such a system;

(2) develop methods of internal controls and accounting by which the Government can assure that payments received through a lockbox system will be promptly and fully credited to the Treasury of the United States;

(3) develop criteria for the adoption of lockbox systems by executive agencies;

(4) analyze the feasibility and costs of operating lockbox systems through the Department of the Treas-

ury, the Federal Reserve Board, or other appropriate executive agencies; and

(5) develop recommendations for the establishment of lockbox systems by executive agencies, with the cost of establishing and operating such systems paid by appropriated funds.

(c) Within 180 days after the date of enactment of this Act, the Secretary shall submit a report on the study conducted under subsection (b) to the President pro tempore of the Senate and the Speaker of the House of Representatives. The report shall describe the findings of the study and contain such recommendations as the Secretary considers appropriate.

(d) Within ninety days after submitting the report required under subsection (c), the Secretary shall prescribe guidelines which specify procedures to be used by executive agencies in determining whether to establish and operate lockbox systems.

(e) Within ninety days after the Secretary prescribes guidelines under subsection (d), the head of each executive agency shall submit to the Secretary a report describing the plans of such agency for the establishment of a lockbox system or specifying the reasons why such a system is not feasible or cost effective for such agency.

United States General Accounting Office

GAO Testimony

For Release
on Delivery
Expected at
10:30 a.m. EDT
Wednesday
July 22, 1987

Cash Management Improvement Act of 1987 (S. 1381)

Statement of
Jeffrey C. Steinhoff, Associate Director,
Accounting and Financial Management Division

Before the
Subcommittee on Government Efficiency,
Federalism, and the District of Columbia,
Senate Committee on Governmental Affairs

GAO/T-AFMD-87-17

Mr. Chairman and Members of the Subcommittee:

We are very pleased to be here today to give our views on the Cash Management Improvement Act of 1987--S. 1381--which would provide legislative changes necessary to improve federal cash management and help ensure equity in funding federal programs administered by the states. The purpose of the bill is to increase the efficiency of efforts to manage cash throughout the government by providing additional procedures and incentives for cash management through

-- the adoption of intergovernmental financing concepts developed by the State/Federal Cash Management Reform Task Force,

-- the establishment of disbursement objectives similar to collection objectives which were mandated in the Deficit Reduction Act of 1984, and

-- the expansion of the use of lockboxes as a means of speeding up the deposit of government collections.

GAO has long called for strengthened federal cash management and fully supports S. 1381. We previously supported the concepts in the bill when they were part of S. 2230, which was

reported on favorably last year by the Senate Governmental Affairs Committee.[1]

We see S. 1381 as an important opportunity to continue the progress already made in better managing the government's financial affairs. We also believe that it is important in another respect; it is a good example of what can be achieved when state and federal representatives work together to solve a long-standing problem.

PAYMENT OF INTEREST: INTERGOVERNMENTAL FINANCING

Section 4 of the bill addresses a long-standing cash management problem in federal programs administered by the states--ensuring that neither party incurs unnecessary interest costs. The concerns became even more intensified during periods of high interest rates and budget constraints. Both federal and state officials have raised objections to the current intergovernmental financing arrangements.

The federal government has been concerned about states drawing down federal funds sooner than necessary to cover disbursements for federal programs, thereby profiting from

[1]Responses to questions in testimony by Charles A. Bowsher, Comptroller General of the United States, before the Senate Governmental Affairs Committee on S. 2230, the Federal Management Reorganization and Cost Control Act of 1986, on May 13, 1986.

interest earned by holding federal funds. Under the Intergovernmental Cooperation Act (31 U.S.C. 6503), the federal government essentially cannot charge the states interest in these cases. To help solve this problem, the federal government developed cash drawdown techniques, whereby states would not receive federal funds until their checks cleared the bank. However, this presented legal problems for many states which have laws requiring that sufficient cash be on hand before checks are issued.

Likewise, the states have complained that they often do not receive federal funds soon enough and must use their own cash to finance federal programs, sometimes waiting several months for reimbursement. When that happens, states cannot charge the federal government for the associated interest costs.

To seek fair and equitable solutions to these problems, and at the urging of members of the Congress, the State/Federal Cash Management Reform Task Force was formed in 1983. Represented are fiscal officials of six states (Virginia, California, Florida, New Jersey, Tennessee, and Wisconsin) and six federal officials from the Office of Management and Budget and the departments of the Treasury and Health and Human Services. The results of 4 years of excellent work by the Task Force are reflected in section 4 of S. 1381.

Section 4 of the bill would amend the Intergovernmental Cooperation Act and establish a set of intergovernmental cash management policies and practices that can (1) govern the exchanges of funds between the federal and state governments and (2) ensure that neither the federal nor state governments benefit or suffer financially as a result of the transfer of cash in support of federal programs--equity is the key.

For example, under section 4:

-- Agency heads are required to minimize the time elapsing between the transfer of funds by Treasury and the issuance of payments by a state. States are also required to minimize the time between the receipt of federal funds and issuance of payments.

-- The Secretary of the Treasury is to issue regulations that require a state to pay interest on federal funds that are received in advance of need. Conversely, if a state disburses its own funds for program purposes in accordance with federal law, regulation, or federal-state agreement, the state is to be paid interest by the federal government.

-- The Secretary of the Treasury is to prescribe the methods of paying interest between the states and the federal

government while ensuring comparable treatment for both parties.

-- The federal government is required to execute grant awards, consistent with program purposes and regulations, on a timely basis to ensure the availability of federal funds when needed by a state to make payments under a federal program. Interest earned by a state on refunds of grant funds is to be returned to the federal government.

The requirements of section 4 apply to all federal programs and supercede any federal law or regulation in effect at the time S. 1381 is enacted. States and the federal government will have 2 years before the interest payment procedures go into effect to give both parties the necessary time to make improvements in cash management practices and procedures and to put into effect the systems needed to implement the interest payment provisions of this section. We have provided a few technical suggestions to the subcommittee for its consideration in finalizing section 4.

We believe the provisions of section 4 are fair to both parties, represent the reasoned judgment of federal and state task force members, and will resolve a long-standing point of contention between the federal government and the states.

FEDERAL DISBURSEMENT OBJECTIVES

We also support section 3 of S. 1381, which provides legislative incentives to help ensure that federal agencies follow sound cash management concepts in disbursing federal funds. These provisions are patterned after those relating to collections in the Deficit Reduction Act of 1984 (31 U.S.C. 3720). This law provided additional tools to the Secretary of the Treasury to help ensure that federal agencies follow sound cash management concepts in collecting and depositing federal funds. For example, Treasury is now permitted to penalize agencies that do not follow its regulations governing collections by assessing an agency for the cost of any losses to the general fund.

The authority in the Deficit Reduction Act of 1984, however, only covers federal collections but does not extend to federal disbursements. Federal disbursements, which exceed a trillion dollars annually, also present significant cash management concerns. We see no reason why cash management principles in the Deficit Reduction Act should not be applied to federal disbursements as well as collections. Section 3 provides the necessary remedies.

Consistent with this concern, we recently testified[2] before the Senate Governmental Affairs Committee on the Prompt Payment Act Amendments of 1987 (S. 328). The Prompt Payment Act, which was passed under the leadership of the committee, provided a strong foundation for making the federal government a more responsible bill payer. It also had the benefit of providing an incentive for agencies to pay their bills when they are due instead of late. However, during a review[3] completed last year on the implementation of the act, we found that about one-fourth of the government's payments were made early, thereby costing the federal government millions of dollars in interest income. Section 3 of S. 1381, in conjunction with the Prompt Payment Act, provides the necessary incentives for agencies to pay their bills on time--neither early nor late.

We offer one technical suggestion. The subcommittee may wish to specify in section 3 of S. 1381 that any interest penalties assessed by Treasury should be paid out of appropriations available for agency operations where possible and therefore not reduce amounts available to fund programs. We understand that a reduction of available program funds has been a concern of the states.

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[2]S. 328, a bill to amend the Prompt Payment Act (GAO/T-AFMD-87-3, March 19, 1987).

[3]Prompt Payment Act: Agencies Have Not Fully Achieved Available Benefits (GAO/AFMD-86-69, August 28, 1986).

NATIONAL LOCKBOX SYSTEMS

Finally, we support section 5, which addresses the improved collection and deposit of government receipts through lockbox systems. Federal receipts are sent to a post office box, processed, and credited to the government's account, thus eliminating deposit delays.

This bill recognizes that a comprehensive study needs to be performed before requiring federal agencies to use lockbox arrangements and calls for Treasury to analyze the feasibility and costs of operating lockbox systems through Treasury, the Federal Reserve, or other appropriate federal agencies.

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Mr. Chairman, this concludes my remarks. We fully support S. 1381 and stand ready to work with the subcommittee as it considers the bill. We would be pleased to respond to any questions you or members of the subcommittee may have at this time.

Cash Management Improvement Act of 1987
Presentation to the Subcommittee
on Government Efficiency, Federalism
and the District of Columbia
by
Frank L. Greathouse
July 22, 1987

For the committee to understand the reason state officials consider the Cash Management Improvement Act of 1987 necessary legislation, one has to explore the history of state and federal cooperation in the late 1960s and early 70s. At that time, the federal government began its expansion of programs to grant more money to state and local governments to help them carry out federal programs. It became apparent that neither the federal or the state and local management and accounting systems were capable of accounting for and reporting on the fiscal transactions to disclose appropriately to federal managers, Congress, and the general public whether the programs were effectively executed.

Over a period of years, federal officials saw a need for better accountability at the state and local level. At the same time, state officials saw a need for better communication and guidelines from the federal government. During this period, an atmosphere of mistrust existed between federal officials and state and local government officials.

Some state officials realized the need for a better method of communication between all levels of government. In the early 1970s, five state officials, including William R. Snodgrass, Tennessee's Comptroller of the Treasury, approached the Comptroller General of the United States, Elmer Staats, about finding a method for the state and local audit community to communicate its needs and concerns to the federal audit community. These meetings led to the organization first of the Southeastern Intergovernmental Audit Forum in federal region four in Atlanta, followed almost immediately by the organization of the National Intergovernmental Audit Forum here in Washington. This movement then led to the organization of intergovernmental audit forums in all ten of the federal regions. These forums continue to be active today.

The audit forums led to a higher level of communication between state and local auditors and their federal counterparts. Many issues relating to the management and audit of federally assisted programs were discussed over the years and led to improved cooperation between state, local, and federal program and fiscal managers.

Along with the development of the forums, and parallel to them, the General Accounting Office began to develop governmental accounting standards. The first edition of Standards for Audits of Government Organizations, Programs, Activities and Functions, better known as the Yellow Book, was published in 1972. The standards were revised in 1981 and are currently being reexamined. Because of the high level of cooperation through the audit forums in the development of the audit standards, and input by state and local governments, the audit standards have been widely accepted.

In the midst of this activity, state fiscal officials began meeting in the early 70s to consider how to standardize accounting and financial management. During this same period, the federal Revenue Sharing Act was passed. Its enactment

required a higher level of financial reporting and auditing by state and local governments.

Also, in the middle 70s, the bond default of New York City and the threatened default in other large cities pointed to a need for state and local governments to improve their financial disclosure and reporting. I should note here that throughout this period, there was no failure in accounting standards; there was instead New York City's failure to use the standards. What was needed in the mid 70s was acceptance and enforcement of existing accounting standards. Because of all these almost simultaneous happenings and because of pressures from the financial community for reform in state and local governmental accounting, the Municipal Finance Officers Association moved to reorganize the National Council on Governmental Accounting and to reexamine the accounting standards. As a result, disclosure guidelines were put in place for the issuance of state and local governments' securities. Also, the State Accounting Project was created to develop the preferred practices of accounting and reporting by states and the National Council on Governmental Accounting, an agency of the Municipal Finance Officers Association, now the Government Finance Officers Association, moved to assist in the creation of the Governmental Accounting Standards Board. All of these described activities led to the development and organization of the Governmental Accounting Standards Board.

State and local governments were having to deal with the federal government, not as an entity, but as a multi-headed Medussa. Each department of the federal government attempted to deal fiscally with its fiscal counterpart in state government. Seldom did the policy setters in the federal government consult with the policy-setting officials in state government. Therefore, not all departments in state government were handling federal funds in the same way. Out of this confusion grew fiscal mismanagement of federally assisted programs at the state and local levels. Cash management of federally assisted programs was not even-handed and was mismanaged both at the federal and state level.

Our experience in Tennessee demonstrates the problem. In 1979, we learned at the National Intergovernmental Audit Forum how the Department of Health and Human Services would like state governments to draw down money. This method was called the delayed drawdown letter of credit. Simply stated, when state-issued checks were paid by the bank, the state could then draw that money down based on a clearing-pattern letter of credit from the federal government. This method actually would have violated the law in many states because until the money is in the bank, a check could not be issued. After attempting through the audit forums and other methods to explain the delayed drawdown letter of credit, Health and Human Services, working with the U. S. Treasury, began to work with program officials in several states. Changing the drawdown method meant a change in the accounting system. Seldom were the policy-making officials such as the state treasurer, the state comptroller, or the governor consulted.

In most state governments, no change in the accounting system can be made without the approval of the appropriate policy-setting officials. In Tennessee, those officials are the Comptroller of the Treasury and the Commissioner of the Department of Finance and Administration.

The Tennessee Department of Human Services in executing the AFDC program began working with the federal Department of Health and Human Services to draw down its funds using the delayed drawdown method. Only accidently did the Tennessee Comptroller of the Treasury learn that the method was being changed.

When my office discovered the change, I immediately reacted by stating that until all departments of the federal government decided to use the same drawdown method or an equitable one, the state of Tennessee would not use this method in any of its programs. Not even the federal Treasury Department could accomplish this type of coordination in the federal system.

On September 24, 1981, I wrote a letter to Mr. David Stockman, Director of the Office of Management and Budget. In this letter, I included several schedules of information on Health and Human Services' method of cash management. I told him that North Carolina, South Carolina, Kentucky, and Tennessee had joined in an effort to look at cash management in government from both the state and federal perspective (copies are attached). I advised Mr. Stockman that in my opinion, the JFMIP should study the equitableness of delayed drawdown before a comprehensive cash management program could be implemented. As president of the National State Auditors Association and chairman of an ad hoc committee of the National Association of State Auditors, Comptrollers and Treasurers, I requested such a study.

The JFMIP made such a study of cash management in Tennessee. It revealed that the state was actually drawing down its money too fast and earning interest in the AFDC and Medicaid programs. On the other hand, the state Departments of Education and Transportation were not drawing down their funds as fast as possible; therefore, the federal government had its cash available longer. The offset much favored the federal government.

Stemming from the Tennessee study, a decision was made to expand the JFMIP study to several other states. It became apparent from these studies that there was a question as to who was profiting from the flow of federal funds into state and local treasuries. The results of these studies pointed to the need for a task force to be organized to study further how to make the flow of funds more equitable. That project was created and was called the State/Federal Cash Reform Task Force.

As an auditor, I believed then that my continued involvement in cash management should stop, and the matter was turned over to a special committee of state people appointed by NASACT. Ed Mazur has been chairman of this committee and will be able to relate to the committee the task force's activities.

I consider this legislation necessary to ensure that in the cash management of federal assistance funds, the federal government never returns to dealing with state governments department by department. The federal government should deal with state government as an entity. There is one federal government to deal with one state government. An example of how this can be successfully accomplished is to examine what caused the enactment of the Single Audit Act of 1984. For years, state auditors had to deal separately with the auditors of every department of the federal government and occasionally with auditors from GAO. Each of the federal departments had a different method and different audit requirements that state auditors had to apply to the audits of federally assisted programs. At one time, there were as many as 90-plus audit guides in existence. Consequently, some programs were audited by several levels of audit organizations, and some were never audited. The GAO put out a report calling attention to the overauditing and gaps in auditing federally assisted programs.

The idea of single audit was developed in an attempt to solve this problem. At that time, the JFMIP again was called upon to make a study. As a result, it was found that single audits were the solution; that is, one audit would suffice for one entity and would satisfy the needs of all federal departments and agencies as well as

state and local governments. The Office of Management and Budget attempted to enforce single audit requirements through Federal Management Circulars. This effort failed abysmally. The state audit community began working with GAO to develop a concept of the Single Audit Act, which was finally enacted in 1984 and which has shown signs of being a tremendous success. Scarce audit resources are now being used efficiently and effectively to accomplish audits of not only federally assisted programs but also the governmental entity itself.

I believe that the Cash Management Improvement Act of 1987 can accomplish the same in the cash management of federally assisted programs executed by state and local governments.

I would like to state in closing that state and local governments are much indebted to the federal government for its role in improving accountability in state and local government. If pressure had not been placed upon state and local governments to improve their accounting systems, management systems, and reporting systems, this improvement may not have happened.

Currently, state officials are greatly concerned that the federal government is failing to do for itself what it has required of state and local governments. Accounting systems in various federal departments and institutions are in disarray. The federal government does not follow generally accepted accounting principles, and its financial statements are not audited. The departments and agencies have no system of financial audit of their operations. Until a recent audit of General Services was completed, no department had had a departmental entity-wide audit. The budget system is inefficient and does not accurately relate to the operations and resulting deficits of the federal government. The federal government does not require of itself the cash management that it requires of state and local government. There needs to be reform in this area. Although this committee does not directly deal with those issues, its members need to be concerned with fiscal reorganization of the federal government. A reorganization would lead to a significant reform in federal accounting, budgeting, and reporting.

As president-elect of GFOA, past president of NSAA, a long-time member of the executive committee of NASACT, and a concerned citizen, I believe the federal government's financial management could be reformed by creating a position for a chief financial officer who would have the authority to make changes in all these areas. NASACT and GFOA have pledged their support to the General Accounting Office and to the President's Council on Integrity and Efficiency in such an effort. The passage by the Senate of SB 1381 is a step in the right direction toward better federal fiscal management. I appreciate the opportunity of appearing here and will be glad to answer any questions or to be available at a later date if you consider it necessary.

National State Auditors Association

OFFICERS AND EXECUTIVE COMMITTEE

President
FRANK L. GREATHOUSE
D[illegible]tor, Division of
[illegible]e Audit
15[illegible] James K. Polk
Office Building
Nashville, TN 37219
(615) 741-1910

President-Elect
DOUGLAS R. NORTON
Auditor General
200 State Capitol
Phoenix, AZ 82007
(602) 255-4385

Secretary-Treasurer
ANTHONY PICCIRILLI
Auditor General
87 Park Street
Providence, RI 02908
(401) 277-2435

Immediate Past President
ROBERT G. CRONSON
Auditor General
Marriott Building
509 South Sixth
Springfield, IL 62701
(217) 782-0803

OTHER MEMBERS
T[illegible]HAS HAYES
A[illegible]or General
925 L Street, Suite 750
Sacramento, CA 95814
(916) 445-0255

GORDON MILBRANDT
Auditor General
State Capitol
Pierre, SD 57501
(605) 773-3595

ELDON STOEHR
Legislative Auditor
Veterans Service Building
Saint Paul, MN 55155
(612) 296-4710

COMMITTEE CHAIRMEN

State Auditor Coordinating Committee (SACC)
ELDON STOEHR
Legislative Auditor
Veterans Service Building
Saint Paul, MN 55155
(612) 296-4710

EDP Audit Committee
J[illegible]HEINRICHER
E[illegible]y State Auditor
Legislative Building
Olympia, WA 98504
(206) 753-2447

State Auditor Training Committee (SATC)
THOMAS HAYES
Auditor General
925 L Street, Suite 750
Sacramento, CA 95814
(916) 445-0255

September 24, 1981

The Honorable David Stockman, Director
Office of Management and Budget
New Executive Office Building
Room 6002
Washington, D. C. 20503

Dear Mr. Stockman:

I am enclosing several schedules of information on the delayed-drawdown letter of credit, which has been suggested as a method of cash management by the U. S. Department of Health and Human Services to be implemented in certain states. The states of North Carolina, South Carolina, Kentucky and Tennessee have joined together in an effort to look at cash management in government from both the state perspective and the federal perspective. A proper examination of cash management at both levels should develop a procedure which would be even-handed for all federal departments and programs instead of having one federal department developing a different type of cash management procedure than other departments.

North Carolina and Tennessee have prepared lists of the federal departments and programs which are involved, with an indication how funds are transferred from the federal government to the state government. These lists are the attached Exhibits A and B.

Tennessee has prepared a schedule of programs which have a cash management method different from that used in the AFDC program, which is subject to the delayed-drawdown process. This schedule is attached as Exhibit C. You will note that under this method reimbursing funds advanced by the state for federal purposes, the state loses in excess of nine million dollars annually. We would be glad to work with the appropriate officials in the federal government to seek a more even-handed method of cash management rather than entering into agreements which are selective and apply only to certain programs—as the current implementation of the delayed-drawdown method would do if it were applied to the AFDC program.

North Carolina and Tennessee have both resisted participation in the program until a more even-handed method of cash management is found. A study of this problem by the JFMIP may be necessary before a comprehensive cash management program is implemented. We fully realize that some states are already using the delayed-drawdown method even though

the method is not equitable and actually may penalize those states. You should also be aware that constitutions and statutes may be violated if states are required to expend funds for programs before funds are available in the state treasuries. Even aside from constitutional and legal considerations, such cash management does not seem to be consistent with good management practices.

As President of the National State Auditors Association and Chairman of an Ad Hoc Committee of the National Association of State Auditors, Comptrollers and Treasurers, I am requesting that the Office of Management and Budget consider this matter, place it on the agenda of the JFMIP, and support the concerned parties, at least the four states mentioned above, in not acquiescing to the letter-of-credit method until their concerns have been considered.

Sincerely,

Frank L. Greathouse
President

FLG/pjr

Attachment

cc: Honorable John J. Lordan, Chief, Financial Management Branch, Office of Management and Budget
Honorable Charles Bowsher, Comptroller General of the United States
Honorable Harold I. Steinberg, Associate Director, Office of Management and Budget
Honorable Susumu Uyeda, Executive Director, Joint Financial Management Improvement Program
Honorable George L. Atkins, Secretary, Department of Finance, Kentucky
Honorable Harlan E. Boyles, State Treasurer, North Carolina
Honorable Grady Patterson, State Treasurer, South Carolina
Honorable Harlan Mathews, State Treasurer, Tennessee

STATE OF NORTH CAROLINA
FEDERAL FUNDS AVAILABILITY
FY 1981-82

EXHIBIT A

DEPARTMENT / PROGRAM	FEDERAL AGENCY	BUDGETED AMOUNT	BASIS RECEIVED	METHOD RECEIVED	FREQUENCY RECEIVED
EDUCATION					
School Food Services	USDA	124,781,862	Adv(R)	LOC	Quarterly
ESEA	Education	135,163,820	Adv	LOC	Monthly
Voc. Education	Education	21,473,998	Adv	LOC	Monthly
Various	Education	1,452,630	Adv	LOC	Monthly
		282,877,310			
JUSTICE					
Medicaid Fraud	Justice	360,000	Adv	LOC	Quarterly
AGRICULTURE					
Various	USDA	2,442,333	Reim	CK/LOC	Monthly
Various	USDA	303,714	Adv	CK	Monthly
		2,746,047			
LABOR					
OSHA and Various	Labor	1,760,360	Reim	LOC	Monthly
OSHA and Various	Labor	222,798	Adv	LOC	Monthly
		1,983,158			
ADMINISTRATION					
Various	Various	2,255,001	Adv	LOC/CK	Various
NATURAL RESOURCES & C.D.					
CETA	Labor	115,523,630	Adv	CK	2 Weekly
Outdoor Rec	Interior	4,266,615	Reim	CK	2 Weekly
Various	Commerce	1,701,602	Adv	LOC	Quarterly
Various	USDA	3,057,278	Adv	LOC	Quarterly
Various	EPA	4,742,845	Adv	LOC	Monthly
Various	HUD	3,155,937	Reim	CK	Monthly
Various	Various	3,446,556	Adv	LOC	Monthly
Various	Various	444,233	Reim	LOC	Various
		136,333,696			
WILDLIFE COMMISSION					
Soil Conservation	USDA	36,000	Reim	CK	Monthly
Various	Interior	2,335,245	Reim	LOC	Monthly
		2,371,245			
DHR-OFFICE OF SECRETARY					
Title XX	HHS	75,619,709	Adv	LOC	As needed
Child Development	ARC	1,560,613	Adv	LOC	Monthly
Health Disabilities	HHS	1,962,380	Adv	LOC	Monthly
Aging	HHS	11,254,238	Adv	LOC	Monthly
Aging	USDA	1,500,266	Adv	LOC	Monthly
Aging	Action	103,924	Adv	CK	Monthly
Aging	Labor	1,441,390	Adv	CK	Monthly
		93,442,520			
DHR-DIV HEALTH SERVICES					
WIC	USDA	34,945,175	Rem(CP)	LOC	Weekly
Water and Soil	EPA	1,793,653	Adv	LOC	Weekly
Crippled Childred	HHS	4,479,193	Adv	LOC	Weekly
Maternal and Child	HHS	8,745,507	Adv	LOC	Weekly
Family Planning	HHS	3,903,305	Adv	LOC	Weekly
Various	HHS	4,986,101	Adv	LOC	Weekly
		58,852,934			
DHR-DIV SOCIAL SERVICES					
Food Stamps	USDA	10,157,596	Adv(R)	LOC	Monthly
AFDC	HHS	123,286,236	Adv	LOC	As needed
Disability Determ.	HHS	8,004,452	Adv	LOC	Monthly
Corps	Labor	442,076	Rem	CK	Monthly
Child Support	HHS	6,599,294	Adv	LOC	Monthly
Various	HHS	4,783,146	Adv	LOC	Monthly
		153,272,800			
DHR-DIV MEDICAL ASSISTANCE					
Medicaid	HHS	383,052,099	Adv	LOC	Weekly

- Continued -

EXHIBIT A

DHR-DIV SERVICES FOR BLIND					
Various	HHS	5,484,961	Adv	LOC	Monthly
DHR-DIV MENTAL HEALTH					
Various	HHS	4,009,482	Rem	LOC	Monthly
DHR-DIV FACILITY SERVICES					
Various	HHS	500,341	Adv	LOC	As needed
DHR-DIV VOC REHABILIATION					
Various	HHS	24,757,987	Adv	LOC	Weekly
COMMERCE					
Small Business Dev	Commerce	70,000	Adv	CK	Quarterly
NASA Technology	NASA	225,000	Reim	CK	Monthly
Energy and Various	Energy	3,530,400	Adv	CK	As needed
		3,825,400			
EMPLOYMENT SECURITY COMM.					
WIN	HHS	3,073,511	Adv	LOC	As needed
Food Stamps	USDA	2,760,526	Adv	LOC	As needed
Unemployment Insurance	Labor	21,160,330	Adv	LOC	Daily
Employment Service	Labor	18,401,465	Adv	LOC	As needed
Various	Labor	1,684,841	Adv	LOC	As needed
		47,080,673			
CULTURAL RESOURCES					
Historic Preservation A & D	Interior	478,420	Rem	CK	Monthly
Historic Preservation S & P	Interior	1,107,320	Adv	CK	Monthly
Arts	Arts & Human	359,080	Rem	CK	Quarterly
Title I and III	HHS	1,652,361	Rem	LOC	Monthly
		3,597,181			
CRIME CONTROL & PUBLIC SAFETY					
Weather Radio	Commerce	30,787	Adv	CK	Monthly
Natural Disaster	HUD	25,000	Adv	LOC	Monthly
LEAA	Justice	3,128,000	Adv	CK	Monthly
Guard and various	Defence	2,345,000	Adv	LOC	Monthly
		5,528,787			
TRANSPORTATION					
Trans. and Construction	Trans	178,589,000	Reim	LOC	Weekly
Gov. Highway Safety	Trans	5,540,236	Reim	LOC	Monthly
Elderly & Handicapped	Trans	600,000	Reim	LOC	Monthly
Rural and Urban Trans	Trans	3,700,000	Reim	LOC	Monthly
Rail Service	Trans	1,200,000	Reim	CK	Monthly
		189,629,236			
TOTAL ALL FEDERAL FUNDS		1,402,069,758			

Total Received on Advance Basis to State	1,020,949,747
Total Received on Advance Basis to State but Reimbursement Basis to Local Govts.	134,939,458
Total Received on Reimbursement Basis to State	246,180,553
	1,402,069,758

NOTES:

Reim - Reimbursement Basis
Adv - Advance Basis
Adv (R) - Advance to State but Reimbursement to Local Govts
Rem (CP) - Modified Checks Paid Method
Budgeted figures based on information prepared by Budget Division Fall 1980.
Above is consolidation of over 300 Federal budget codes and does not include funds deposited directly to a General Fund budget code
Funds received on advance basis must be spent within 3 days of receipt in most cases

Prepared by Department of State Treasurer, September 1981

AVAILABILITY OF FEDERAL FUNDS

Department	Budgeted Federal Revenue 1981-82		Source	Amount Received on Letter of Credit	Amount Received on Reimbursement Basis	When Reimbursed - in Relationship to When Payments are Made
Comptroller	$ 125,000		HHS	$	$ 125,000	As needed
PSC	122,800		DOT		122,800	Advanced semi-annually
Health Planning & Resource Serv.	493,600		HHS		493,600	15th following month
CSA	30,159,100		DOE, CSA, HHS	30,159,100		Letter of Credit
Highway Safety	4,289,400		DOT		4,289,400	15th day following month
LEPA	6,695,000		LEAA		6,695,000	15th & 30th of month
State and Local Planning	940,700		HUD, EDA, HHS		940,700	Based on % comp. of project
Tn. Children's Commission	69,500		ARC		69,500	Quarterly
Aging	12,269,600		USDA	12,269,600		When warrant is issued
Human Development	115,600		EEOC	115,600		In advance
Arts Commission	517,300		Endowment for Arts		517,300	Quarterly advance
THDA	14,972,700		HUD	14,972,700		In advance
Energy Authority	2,731,400		DOE		2,731,400	15th following month
Personnel	330,300		IPA		330,300	Qtr. Fed. Status Report
* Education	254,505,000		Education	170,370,600	84,134,400	Wire Trans. weekly
MH/MR	4,774,500		HHS	4,774,500		Weekly
Medicaid	327,336,200		HHS	327,336,200		Weekly
FH	48,333,500		HHS	48,242,900	90,600	Weekly
Emp. Security	129,599,100	1	Labor	129,599,100		Daily wire trans.
PHS	95,660,300		HHS	95,660,300		Weekly
AFDC	62,131,000		HHS	62,131,000		Weekly
Attorney General	101,900		Justice		101,900	Quarterly
Military	9,722,000		NAO, FENA		9,722,000	30 days after mo.
Agriculture	1,544,400		USDA	43,750	1,500,700	Quarterly
** Conservation	10,263,300		Interior		10,263,300	15th following mo.
TWRA	2,934,900		Interior		2,934,900	Quarterly
E & CD	1,189,100		EDA, AR		1,189,100	Quarterly
Labor	1,432,600		Labor		1,432,600	Monthly adv.
*** Transportation	269,172,000		FHA		269,172,000	Request made on 1st Thurs. following end of month, payment following Monday
	$1,292,531,800			$895,675,300	$396,856,500	
Less: Trust Fund-Emp. Security	(129,599,100)	1		(129,599,100)		
Net Federal Funds excluding trust	$1,162,932,700			$ 766,076,200	$396,856,500	

*Education is paid daily and collected weekly
**Conservation is paid as needed and collected quarterly
***Transportation is paid daily

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EXHIBIT B

ANALYSIS OF CASH MANAGEMENT
STATE OF TENNESSEE
AS OF JUNE 30, 1981
(FOR SELECTED DEPARTMENTS OR AGENCIES)

Department	Estimated Annual Reimbursement (See A Below)	P = PRINCIPAL Average Monthly (M) or Quarterly (Q) Drawdown	T = TIME Weighted Average O/S Days Before Drawdown (See B Below)	R = RATE Weighted Average Rate on Investments Made (Note 1)	I = INTEREST Monthly (M) or Quarterly (Q) Interest Loss I = prt	Annualized Interest Loss (I x Factor) (See C Below)
Highway Safety	$ 4,289,400	$ 357,450 (M)	24.68	13.79%	$ 3,379 (M)	$ 40,555
Military	5,136,700	428,058 (M)	84.02	13.79	13,776 (M)	165,311
Education	254,505,000	21,208,750 (M)	59.8	13.79	485,822 (M)	5,829,868
Conservation	7,906,207	1,976,552 (Q)	142.8	13.79	108,118 (Q)	432,472
Transportation	269,172,000	22,431,000 (M)	24.79	13.79	213,004 (M)	2,556,043
Law Enforcement Planning	7,800,000	650,000 (M)	29.67	13.79	7,387 (M)	88,649
					Total	$9,112,898

Assumptions:

A) In some cases to arrive at this figure, the State agency or department annualized their estimate or reimbursement for the state fiscal year ended June 30, 1982 by using a representative month or quarter's figures during the prior fiscal year and multiplying by the appropriate number of months or quarters to arrive at an annual estimate of reimbursement.

B) The average outstanding days calculation was weighted based on the amount in dollars ($) that each expenditure during the representative time period was of the total reimbursement for the sample month or quarter selected.

C) Monthly factor is 12; Quarterly factor is four.

NOTE 1: Weighted Average Rate on Investments made for the fiscal year ended June 30, 1981 (Attachment 1) was taken from the Treasurer's Report, 1981, State of Tennessee, Analysis of Cash Management.

TREASURY ACCOUNTING
CASH MANAGEMENT ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 1981

MONTH	AVERAGE INVESTMENTS			AVERAGE RATES ON INVESTMENTS MADE		WEIGHTED AVERAGE RATE ON INVESTMENTS MADE	WEIGHTED AVERAGE CUMULATIVE RATE OF RETURN
	TIME DEPOSITS	REPURCHASES	TOTAL	TIME DEPOSITS	REPURCHASES		
July, 1980	$ 630,816,419	$ 98,330,000	$ 729,146,419	8.22%	8.61%	8.45%	10.78%
August, 1980	658,770,451	149,888,333	808,658,784	9.08%	9.20%	9.16%	10.32%
September, 1980	626,389,000	90,721,000	717,110,000	10.54%	10.73%	10.69%	10.51%
October, 1980	592,060,613	105,440,322	697,500,935	11.74%	12.15%	12.04%	10.78%
November, 1980	597,447,133	82,653,333	680,100,466	14.06%	14.50%	14.30%	11.37%
December, 1980	609,021,129	53,965,105	662,986,234	16.45%	18.33%	17.22%	12.67%
January, 1981	615,625,193	72,203,552	687,828,745	15.07%	18.03%	16.55%	13.65%
February, 1981	586,688,500	63,773,571	650,462,071	14.92%	15.77%	15.41%	13.69%
March, 1981	548,920,355	63,403,226	612,323,581	14.20%	14.27%	14.25%	13.74%
April, 1981	540,717,129	64,056,667	604,773,796	13.85%	14.97%	14.43%	13.83%
May, 1981	541,360,677	72,925,806	614,286,483	15.51%	16.32%	15.98%	14.10%
June, 1981	559,380,999	56,420,000	615,800,999	16.33%	17.91%	17.01%	14.58%
Avg. Per Month	592,266,466	81,148,409	673,414,875	13.33%	14.23%	13.79%	12.50%

7/21/81

EXHIBIT C
Page 2

National State Auditors Association

OFFICERS AND EXECUTIVE COMMITTEE

President
FRANK L. GREATHOUSE
Director, Division of State Audit
1500 James K. Polk Office Building
Nashville, TN 37219
(615) 741-1910

President-Elect
DOUGLAS R. NORTON
Auditor General
200 State Capitol
Phoenix, AZ 82007
(602) 255-4185

Secretary-Treasurer
ANTHONY PICCIRILLI
Auditor General
87 Park Street
Providence, RI 02908
(401) 277-2435

Immediate Past President
ROBERT G. CRONSON
Auditor General
Marriott Building
509 South Sixth
Springfield, IL 62701
(217) 782-0803

OTHER MEMBERS
THOMAS HAYES
Auditor General
925 L Street, Suite 750
Sacramento, CA 95814
(916) 445-0255

GORDON MILBRANDT
Auditor General
State Capitol
Pierre, SD 57501
(605) 773-3595

ELDON STOEHR
Legislative Auditor
Veterans Service Building
Saint Paul, MN 55155
(612) 296-4710

COMMITTEE CHAIRMEN

State Auditor Coordinating Committee (SACC)
ELDON STOEHR
Legislative Auditor
Veterans Service Building
Saint Paul, MN 55155
(612) 296-4710

EDP Audit Committee
K HEINRICHER
City State Auditor
Legislative Building
Olympia, WA 98504
(206) 753-2447

State Auditor Training Committee (SATC)
THOMAS HAYES
Auditor General
925 L Street, Suite 750
Sacramento, CA 95814
(916) 445-0255

September 24, 1981

The Honorable Richard S. Schweiker
Secretary, U. S. Department of Health
and Human Services
330 Independence Avenue
Washington, D. C. 20201

Dear Secretary Schweiker:

The National State Auditors Association and an Ad Hoc Committee of the National Association of State Auditors, Comptrollers and Treasurers (NASACT) are concerned about the U. S. Department of Health and Human Services' implementation of delayed-drawdown procedure against letters of credit in the AFDC program. We have written a letter to David Stockman, Director of the Office of Management and Budget, asking that this matter be placed on the agenda of the JFMIP for consideration.

I am also aware that George Atkins, Secretary, Department of Finance, Commonwealth of Kentucky, and The Honorable James B. Hunt, Jr., Governor of North Carolina, have written you letters concerning the matter. The states of Tennessee and South Carolina are resisting attempts by your financial management personnel to implement the delayed-drawdown procedures. The NASACT organization representing fiscal officers in all states support a resolution of this matter.

The above-mentioned four states are used as examples in an effort to work with the Office of Management and Budget, the U. S. Treasury Department, and the U. S. Department of Health and Human Services to develop an even-handed method of cash management which could be used by all federal departments in their management of the federally assisted programs of state governments. We would appreciate your department assisting us in cooperation with the proper federal official in the Office of Management and Budget, the Treasury Department, and the General Accounting Office to develop equitable cash management procedures.

I appreciate your kind attention to this matter.

Sincerely,

Frank L. Greathouse
President

FLG/pjr

cc: The Honorable Charles Bowsher
The Honorable David Stockman

National State Auditors Association

OFFICERS AND EXECUTIVE COMMITTEE

President
FRANK L. GREATHOUSE
[illegible]tor, Division of
[illegible]ate Audit
1300 James K. Polk
Office Building
Nashville, TN 37219
(615) 741-1910

President-Elect
DOUGLAS R. NORTON
Auditor General
200 State Capitol
Phoenix, AZ 85007
(602) 255-4385

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509 South Sixth
Springfield, IL 62701
(217) 782-0803

OTHER MEMBERS
[illegible]MAS HAYES
Auditor General
925 L Street, Suite 750
Sacramento, CA 95814
(916) 445-0255

GORDON MILBRANDT
Auditor General
State Capitol
Pierre, SD 57501
(605) 773-3595

ELDON STOEHR
Legislative Auditor
Veterans Service Building
Saint Paul, MN 55155
(612) 296-4710

COMMITTEE CHAIRMEN

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Veterans Service Building
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EDP Audit Committee
[illegible] HEINRICHER
[illegible]ty State Auditor
Legislative Building
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(206) 753-2447

State Auditor Training Committee (SATC)
THOMAS HAYES
Auditor General
925 L Street, Suite 750
Sacramento, CA 95814
(916) 445-0255

September 24, 1981

The Honorable Charles Bowsher
Comptroller General of the United States
U. S. General Accounting Office
441 G Street, N. W.
Washington, D. C. 20548

Dear General Bowsher:

I am enclosing copies of correspondence with the Office of Management and Budget and the U. S. Department of Health and Human Services concerning delayed-drawdown letters of credit, which have been used in some states' AFDC programs. Our concern is that this method of cash management is not even-handed and that cash management needs to be looked at by all federal departments, with the aim of finding an equitable method which could be used by all federal departments and programs.

I have requested that the matter be referred to the JFMIP for research and consideration before such procedures are mandated by the U. S. Department of Health and Human Services.

We respectfully request your support as a member of the JFMIP.

Sincerely,

Frank L. Greathouse
President

FLG/pjr

Enclosures

cc: The Honorable Richard S. Schweiker
The Honorable David Stockman

National State Auditors Association

OFFICERS AND EXECUTIVE COMMITTEE

President
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ate Audit
, James K. Polk
Office Building
Nashville, TN 37219
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September 24, 1981

The Honorable David Stockman, Director
Office of Management and Budget
New Executive Office Building
Room 6002
Washington, D. C. 20503

Dear Mr. Stockman:

I am enclosing several schedules of information on the delayed-drawdown letter of credit, which has been suggested as a method of cash management by the U. S. Department of Health and Human Services to be implemented in certain states. The states of North Carolina, South Carolina, Kentucky and Tennessee have joined together in an effort to look at cash management in government from both the state perspective and the federal perspective. A proper examination of cash management at both levels should develop a procedure which would be even-handed for all federal departments and programs instead of having one federal department developing a different type of cash management procedure than other departments.

North Carolina and Tennessee have prepared lists of the federal departments and programs which are involved, with an indication how funds are transferred from the federal government to the state government. These lists are the attached Exhibits A and B.

Tennessee has prepared a schedule of programs which have a cash management method different from that used in the AFDC program, which is subject to the delayed-drawdown process. This schedule is attached as Exhibit C. You will note that under this method reimbursing funds advanced by the state for federal purposes, the state loses in excess of nine million dollars annually. We would be glad to work with the appropriate officials in the federal government to seek a more even-handed method of cash management rather than entering into agreements which are selective and apply only to certain programs--as the current implementation of the delayed-drawdown method would do if it were applied to the AFDC program.

North Carolina and Tennessee have both resisted participation in the program until a more even-handed method of cash management is found. A study of this problem by the JFMIP may be necessary before a comprehensive cash management program is implemented. We fully realize that some states are already using the delayed-drawdown method even though

the method is not equitable and actually may penalize those states. You should also be aware that constitutions and statutes may be violated if states are required to expend funds for programs before funds are available in the state treasuries. Even aside from constitutional and legal considerations, such cash management does not seem to be consistent with good management practices.

As President of the National State Auditors Association and Chairman of an Ad Hoc Committee of the National Association of State Auditors, Comptrollers and Treasurers, I am requesting that the Office of Management and Budget consider this matter, place it on the agenda of the JFMIP, and support the concerned parties, at least the four states mentioned above, in not acquiescing to the letter-of-credit method until their concerns have been considered.

Sincerely,

Frank L. Greathouse
President

FLG/pjr

Attachment

cc: Honorable John J. Lordan, Chief, Financial Management Branch, Office of Management and Budget
Honorable Charles Bowsher, Comptroller General of the United States
Honorable Harold I. Steinberg, Associate Director, Office of Management and Budget
Honorable Susumu Uyeda, Executive Director, Joint Financial Management Improvement Program
Honorable George L. Atkins, Secretary, Department of Finance, Kentucky
Honorable Harlan E. Boyles, State Treasurer, North Carolina
Honorable Grady Patterson, State Treasurer, South Carolina
Honorable Harlan Mathews, State Treasurer, Tennessee

STATE OF NORTH CAROLINA
FEDERAL FUNDS AVAILABILITY
FY 1981-82

EXHIBIT 9

AGENCY / PROGRAM	FEDERAL AGENCY	BUDGETED AMOUNT	BASIS RECEIVED	METHOD RECEIVED	FREQUENCY RECEIVED
EDUCATION					
School Food Services	USDA	124,781,862	Adv(R)	LOC	Quarterly
ESEA	Education	135,163,820	Adv	LOC	Monthly
Voc. Education	Education	21,473,998	Adv	LOC	Monthly
Various	Education	1,452,620	Adv	LOC	Monthly
		282,877,300			
JUSTICE					
Medicaid Fraud	Justice	360,000	Adv	LOC	Quarterly
AGRICULTURE					
Various	USDA	2,442,333	Reim	CK/LOC	Monthly
Various	USDA	303,714	Adv	CK	Monthly
		2,746,047			
LABOR					
OSHA and Various	Labor	1,760,360	Reim	LOC	Monthly
OSHA and Various	Labor	222,798	Adv	LOC	Monthly
		1,983,158			
ADMINISTRATION					
Various	Various	2,255,001	Adv	LOC/CK	Various
NATURAL RESOURCES & C.D.					
CETA	Labor	115,523,630	Adv	CK	2 Weekly
Outdoor Rec	Interior	4,266,615	Reim	CK	2 Weekly
Various	Commerce	1,701,602	Adv	LOC	Quarterly
Various	USDA	3,057,278	Adv	LOC	Quarterly
Various	EPA	4,742,845	Adv	LOC	Monthly
Various	HUD	3,155,937	Reim	CK	Monthly
Various	Various	3,446,556	Adv	LOC	Monthly
Various	Various	444,233	Reim	LOC	Various
		136,333,696			
WILDLIFE COMMISSION					
Soil Conservation	USDA	36,000	Reim	CK	Monthly
Various	Interior	2,335,245	Reim	LOC	Monthly
		2,371,245			
DHR-OFFICE OF SECRETARY					
Title XX	HHS	75,619,709	Adv	LOC	As needed
Child Development	ARC	1,560,613	Adv	LOC	Monthly
Health Disabilities	HHS	1,962,380	Adv	LOC	Monthly
Aging	HHS	11,254,238	Adv	LOC	Monthly
Aging	USDA	1,500,266	Adv	LOC	Monthly
Aging	Action	103,924	Adv	CK	Monthly
Aging	Labor	1,441,390	Adv	CK	Monthly
		93,442,520			
DHR-DIV HEALTH SERVICES					
WIC	USDA	34,945,175	Rem(CP)	LOC	Weekly
Water and Soil	EPA	1,793,653	Adv	LOC	Weekly
Crippled Childred	HHS	4,479,193	Adv	LOC	Weekly
Maternal and Child	HHS	8,745,507	Adv	LOC	Weekly
Family Planning	HHS	3,903,305	Adv	LOC	Weekly
Various	HHS	4,986,101	Adv	LOC	Weekly
		58,852,934			
DHR-DIV SOCIAL SERVICES					
Food Stamps	USDA	10,157,596	Adv(R)	LOC	Monthly
AFDC	HHS	123,286,236	Adv	LOC	As needed
Disability Determ.	HHS	8,004,452	Adv	LOC	Monthly
Job Corps	Labor	442,076	Rem	CK	Monthly
Child Support	HHS	6,599,294	Adv	LOC	Monthly
Various	HHS	4,783,146	Adv	LOC	Monthly
		153,272,800			
DHR-DIV MEDICAL ASSISTANCE					
Medicaid	HHS	383,067,099	Adv	LOC	Weekly

- Continued -

EXHIBIT A

DHR-DIV SERVICES FOR BLIND					
Various	HHS	5,[illegible],861	Adv	LOC	[illegible]
DHR-DIV MENTAL HEALTH					
Various	HHS	4,098,482	Rem	LOC	Monthly
DHR-DIV FACILITY SERVICES					
Various	HHS	900,341	Adv	LOC	As needed
DHR-DIV VOC REHABILITATION					
Various	HHS	24,757,987	Adv	LOC	Weekly
COMMERCE					
Small Business Dev	Commerce	70,000	Adv	CK	Quarterly
NASA Technology	NASA	225,000	Reim	CK	Monthly
Energy and Various	Energy	3,530,400	Adv	CK	As needed
		3,825,400			
EMPLOYMENT SECURITY COMM.					
WIN	HHS	3,073,511	Adv	LOC	As needed
Food Stamps	USDA	2,760,526	Adv	LOC	As needed
Unemployment Insurance	Labor	21,160,330	Adv	LOC	Daily
Employment Service	Labor	18,401,465	Adv	LOC	As needed
Various	Labor	1,684,841	Adv	LOC	As needed
		47,080,673			
CULTURAL RESOURCES					
Historic Preservation A & D	Interior	478,420	Rem	CK	Monthly
Historic Preservation S & P	Interior	1,107,320	Adv	CK	Monthly
Arts	Arts & Human	359,080	Rem	CK	Quarterly
Title I and III	HHS	1,652,361	Rem	LOC	Monthly
		3,597,181			
CRIME CONTROL & PUBLIC SAFETY					
Weather Radio	Commerce	30,787	Adv	CK	Monthly
Natural Disaster	HUD	25,000	Adv	LOC	Monthly
LEAA	Justice	3,128,000	Adv	CK	Monthly
Guard and various	Defence	2,345,000	Adv	LOC	Monthly
		5,528,787			
TRANSPORTATION					
Trans. and Construction	Trans	178,589,000	Reim	LOC	Weekly
Gov. Highway Safety	Trans	5,540,256	Reim	LOC	Monthly
Elderly & Handicapped	Trans	600,000	Reim	LOC	Monthly
Rural and Urban Trans	Trans	3,700,000	Reim	LOC	Monthly
Rail Service	Trans	1,200,000	Reim	CK	Monthly
		189,629,256			
TOTAL ALL FEDERAL FUNDS		1,402,069,758			

Total Received on Advance Basis to State	1,020,949,747
Total Received on Advance Basis to State but Reimbursement Basis to Local Govts.	134,939,458
Total Received on Reimbursement Basis to State	246,180,553
	1,402,069,758

NOTES:
- Reim - Reimbursement Basis
- Adv - Advance Basis
- Adv (R) - Advance to State but Reimbursement to Local Govts
- Rem (CP) - Modified Checks Paid Method
- Budgeted figures based on information prepared by Budget Division Fall 1980.
- Above is consolidation of over 300 Federal budget codes and does not include funds deposited directly to a General Fund budget code
- Funds received on advance basis must be spent within 3 days of receipt in most cases

Prepared by Department of State Treasurer, September 1981

AVAILABILITY OF FEDERAL FUNDS

Department	Budgeted Federal Revenue 1981-82		Source	Amount Received on Letter of Credit	Amount Received on Reimbursement Basis	When Reimbursed - in Relationship to When Payments are Made
Comptroller	$ 125,000		HHS	$	$ 125,000	As needed
PSC	122,800		DOT		122,800	Advanced semi-annually
Health Planning & Resource Serv.	493,600		HHS		493,600	15th following month
CSA	30,159,100		DOE, CSA, HHS	30,159,100		Letter of Credit
Highway Safety	4,289,400		DOT		4,289,400	15th day following month
LEPA	6,695,000		LEAA		6,695,000	15th & 30th of month
State and Local Planning	940,700		HUD, EDA, HHS		940,700	Based on % comp. of project
Tn. Children's Commission	69,500		ARC		69,500	Quarterly
Aging	12,269,600		USDA	12,269,600		When warrant is issued
Human Development	115,600		EEOC	115,600		In advance
Arts Commission	517,300		Endowment for Arts		517,300	Quarterly advance
THDA	14,972,700		HUD	14,972,700		In advance
Energy Authority	2,731,400		DOE		2,731,400	15th following month
Personnel	330,300		IPA		330,300	Qtr. Fed. Status Report
* Education	254,505,000		Education	170,370,600	84,134,400	Wire Trans. weekly
MH/MR	4,774,500		HHS	4,774,500		Weekly
Medicaid	327,336,200		HHS	327,336,200		Weekly
PH	48,333,500		HHS	48,242,900	90,600	Weekly
Emp. Security	129,599,100	1	Labor	129,599,100		Daily wire trans.
PHS	95,660,300		HHS	95,660,300		Weekly
AFDC	62,131,000		HHS	62,131,000		Weekly
Attorney General	101,900		Justice		101,900	Quarterly
Military	9,722,000		NAO, FENA		9,722,000	30 days after mo.
Agriculture	1,544,600		USDA	43,750	1,500,700	Quarterly
** Conservation	10,263,300		Interior		10,263,300	15th following mo.
TWRA	2,934,900		Interior		2,934,900	Quarterly
E & CD	1,189,100		EDA, AR		1,189,100	Quarterly
Labor	1,432,600		Labor		1,432,600	Monthly adv.
*** Transportation	269,172,000		FHA		269,172,000	Request made on 1st Thurs. following end of month, payment following Monday
	$1,292,531,800			$895,675,300	$396,856,500	
Less: Trust Fund-Emp. Security	(129,599,100)	1		(129,599,100)		
Net Federal Funds excluding trust	$1,162,932,700			$ 766,076,200	$396,856,500	

*Education is paid daily and collected weekly
**Conservation is paid as needed and collected quarterly
***Transportation is paid daily

EXHIBIT D

ANALYSIS OF CASH MANAGEMENT
STATE OF TENNESSEE
AS OF JUNE 30, 1981
(FOR SELECTED DEPARTMENTS OR AGENCIES)

Department	Estimated Annual Reimbursement (See A Below)	P = PRINCIPAL Average Monthly (M) or Quarterly (Q) Drawdown	T = TIME Weighted Average O/S Days Before Drawdown (See B Below)	R = RATE Weighted Average Rate on Investments Made (Note 1)	I = INTEREST Monthly (M) or Quarterly (Q) Interest Loss I = prt	Annualized Interest Loss (I x Factor) (See C Below)
Highway Safety	$ 4,289,400	$ 357,450 (M)	24.68	13.79%	$ 3,379 (M)	$ 40,555
Military	5,136,700	428,058 (M)	84.02	13.79	13,776 (M)	165,311
Education	254,505,000	21,208,750 (M)	59.8	13.79	485,822 (M)	5,829,868
Conservation	7,906,207	1,976,552 (Q)	142.8	13.79	108,118 (Q)	432,472
Transportation	269,172,000	22,431,000 (M)	24.79	13.79	213,004 (M)	2,556,043
Law Enforcement Planning	7,800,000	650,000 (M)	29.67	13.79	7,387 (M)	88,649
					Total	$9,112,898

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Assumptions:

A) In some cases to arrive at this figure, the State agency or department annualized their estimate or reimbursement for the state fiscal year ended June 30, 1982 by using a representative month or quarter's figures during the prior fiscal year and multiplying by the appropriate number of months or quarters to arrive at an annual estimate of reimbursement.

B) The average outstanding days calculation was weighted based on the amount in dollars ($) that each expenditure during the representative time period was of the total reimbursement for the sample month or quarter selected.

C) Monthly factor is 12; Quarterly factor is four.

NOTE 1: Weighted Average Rate on Investments made for the fiscal year ended June 30, 1981 (Attachment 1) was taken from the Treasurer's Report, 1981, State of Tennessee, Analysis of Cash Management.

EXHIBIT C
Page 1

TREASURY ACCOUNTING
CASH MANAGEMENT ANALYSIS
FOR THE FISCAL YEAR ENDED JUNE 30, 1981

MONTH	AVERAGE INVESTMENTS			AVERAGE RATES ON INVESTMENTS MADE		WEIGHTED AVERAGE RATE ON INVESTMENTS MADE	WEIGHTED AVERAGE CUMULATIVE RATE OF RETURN
	TIME DEPOSITS	REPURCHASES	TOTAL	TIME DEPOSITS	REPURCHASES		
July, 1980	$ 630,816,419	$ 98,330,000	$ 729,146,419	8.22%	8.61%	8.45%	10.78%
August, 1980	658,770,451	149,888,333	808,658,784	9.08%	9.20%	9.16%	10.32%
September, 1980	626,389,000	90,721,000	717,110,000	10.54%	10.73%	10.69%	10.51%
October, 1980	592,060,613	105,440,322	697,500,935	11.74%	12.15%	12.04%	10.78%
November, 1980	597,447,133	82,653,333	680,100,466	14.06%	14.50%	14.30%	11.37%
December, 1980	609,021,129	53,965,105	662,986,234	16.45%	18.33%	17.22%	12.67%
January, 1981	615,625,193	72,203,552	687,828,745	15.07%	18.03%	16.55%	13.65%
February, 1981	586,688,500	63,773,571	650,462,071	14.92%	15.77%	15.41%	13.69%
March, 1981	548,920,355	63,403,226	612,323,581	14.20%	14.27%	14.25%	13.74%
April, 1981	540,717,129	64,056,667	604,773,796	13.85%	14.97%	14.43%	13.83%
May, 1981	541,360,677	72,925,806	614,286,483	15.51%	16.32%	15.98%	14.10%
June, 1981	559,380,999	56,420,000	615,800,999	16.33%	17.91%	17.01%	14.58%
Avg. Per Month	592,266,466	81,148,409	673,414,875	13.33%	14.23%	13.79%	12.50%

RHS
7/21/81

EXHIBIT C
Page 2

National State Auditors Association

OFFICERS AND EXECUTIVE COMMITTEE

President
FRANK L. GREATHOUSE
Director, Division of
State Audit
James K. Polk
Office Building
Nashville, TN 37219
(615) 741-1910

President-Elect
DOUGLAS R. NORTON
Auditor General
200 State Capitol
Phoenix, AZ 82007
(602) 255-4385

Secretary-Treasurer
ANTHONY PICCIRILLI
Auditor General
87 Park Street
Providence, RI 02908
(401) 277-2435

Immediate Past President
ROBERT G. CRONSON
Auditor General
Marriott Building
509 South Sixth
Springfield, IL 62701
(217) 782-0803

OTHER MEMBERS
THOMAS HAYES
Auditor General
925 L Street, Suite 750
Sacramento, CA 95814
(916) 445-0255

GORDON MILBRANDT
Auditor General
State Capitol
Pierre, SD 57501
(605) 773-3595

ELDON STOEHR
Legislative Auditor
Veterans Service Building
Saint Paul, MN 55155
(612) 296-4710

COMMITTEE CHAIRMEN

State Auditor Coordinating Committee (SACC)
ELDON STOEHR
Legislative Auditor
Veterans Service Building
Saint Paul, MN 55155
(612) 296-4710

EDP Audit Committee
JACK HEINRICHER
State Auditor
Legislative Building
Olympia, WA 98504
(206) 753-2447

State Auditor Training Committee (SATC)
THOMAS HAYES
Auditor General
925 L Street, Suite 750
Sacramento, CA 95814
(916) 445-0255

September 24, 1981

The Honorable Richard S. Schweiker
Secretary, U. S. Department of Health
and Human Services
330 Independence Avenue
Washington, D. C. 20201

Dear Secretary Schweiker:

The National State Auditors Association and an Ad Hoc Committee of the National Association of State Auditors, Comptrollers and Treasurers (NASACT) are concerned about the U. S. Department of Health and Human Services' implementation of delayed-drawdown procedure against letters of credit in the AFDC program. We have written a letter to David Stockman, Director of the Office of Management and Budget, asking that this matter be placed on the agenda of the JFMIP for consideration.

I am also aware that George Atkins, Secretary, Department of Finance, Commonwealth of Kentucky, and The Honorable James B. Hunt, Jr., Governor of North Carolina, have written you letters concerning the matter. The states of Tennessee and South Carolina are resisting attempts by your financial management personnel to implement the delayed-drawdown procedures. The NASACT organization representing fiscal officers in all states support a resolution of this matter.

The above-mentioned four states are used as examples in an effort to work with the Office of Management and Budget, the U. S. Treasury Department, and the U. S. Department of Health and Human Services to develop an even-handed method of cash management which could be used by all federal departments in their management of the federally assisted programs of state governments. We would appreciate your department assisting us in cooperation with the proper federal official in the Office of Management and Budget, the Treasury Department, and the General Accounting Office to develop equitable cash management procedures.

I appreciate your kind attention to this matter.

Sincerely,

Frank L. Greathouse
President

FLG/pjr

cc: The Honorable Charles Bowsher
The Honorable David Stockman

National State Auditors Association

OFFICERS AND EXECUTIVE COMMITTEE

President
FRANK L. GREATHOUSE
Director, Division of
State Audit
300 James K. Polk
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Nashville, TN 37219
(615) 741-1910

President-Elect
DOUGLAS R. NORTON
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Phoenix, AZ 82007
(602) 255-4385

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OTHER MEMBERS
THOMAS HAYES
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925 L Street, Suite 750
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State Capitol
Pierre, SD 57501
(605) 773-3595

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Veterans Service Building
Saint Paul, MN 55155
(612) 296-4710

COMMITTEE CHAIRMEN

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JACK HEINRICHER
City State Auditor
Legislative Building
Olympia, WA 98504
(206) 753-2447

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THOMAS HAYES
Auditor General
925 L Street, Suite 750
Sacramento, CA 95814
(916) 445-0255

September 24, 1981

The Honorable Charles Bowsher
Comptroller General of the United States
U. S. General Accounting Office
441 G Street, N. W.
Washington, D. C. 20548

Dear General Bowsher:

I am enclosing copies of correspondence with the Office of Management and Budget and the U. S. Department of Health and Human Services concerning delayed-drawdown letters of credit, which have been used in some states' AFDC programs. Our concern is that this method of cash management is not even-handed and that cash management needs to be looked at by all federal departments, with the aim of finding an equitable method which could be used by all federal departments and programs.

I have requested that the matter be referred to the JFMIP for research and consideration before such procedures are mandated by the U. S. Department of Health and Human Services.

We respectfully request your support as a member of the JFMIP.

Sincerely,

Frank L. Greathouse
President

FLG/pjr

Enclosures

cc: The Honorable Richard S. Schweiker
The Honorable David Stockman

TESTIMONY BY

EDWARD J. MAZUR
COMPTROLLER
COMMONWEALTH OF VIRGINIA
AND
CO-CHAIRMAN OF THE
STATE/FEDERAL CASH MANAGEMENT
REFORM TASK FORCE

SPEAKING ON BEHALF OF
NATIONAL ASSOCIATION OF STATE
AUDITORS, COMPTROLLERS AND TREASURERS

BEFORE THE
SUBCOMMITTEE ON GOVERNMENT EFFICIENCY,
FEDERALISM AND THE DISTRICT OF COLUMBIA

OF THE
COMMITTEE ON GOVERNMENTAL AFFAIRS

U.S. SENATE

JULY 22, 1987

MR. CHAIRMAN, MEMBERS OF THE COMMITTEE, my name is Edward J. Mazur. I am the Comptroller of the Commonwealth of Virginia. I appreciate the opportunity to address you this morning and I want to thank you for introducing the intergovernmental financing portions of S.1381. These provisions are contained in Section 4 of the bill.

As co-chairman of the State/Federal Cash Management Reform Task Force, I am especially gratified to appear before you today, because S.1381 embodies concepts agreed to by the task force after four years of striving to develop a fair approach to the exchange of funds between the federal government and the states. I urge the subcommittee to approve these concepts.

The concepts approved by the task force, and contained in S.1381, are designed to make sure there are no winners and no losers in the exchange of funds for joint state/federal programs. Both the federal government and the states are to minimize the time between the transfer of funds to the states and the time when the funds are needed by the states. States are assured that they will have federal funds on hand to meet the requirements of their own laws and regulations. To encourage compliance with these policies, the bill provides for the federal government and the states to pay each other interest. In general, this would occur either when states hold federal cash while awaiting the clearance of disbursements or when states use their funds in advance of receiving federal funds. I want to stress, however, that the cornerstone of this legislation is the achievement of timeliness and equity in the transfer of funds, not the exchange of interest. Interest exchange is simply designed to be an incentive for one level of government to be evenhanded in its fiscal dealings with another level of government. In its work, the task force tried to remember that the same taxpayers fill federal and state coffers, and our primary objective was to serve them well.

A number of points should be made about the relationship between the drawdown of federal funds and the interest exchange provision. First, there is more than one option that a state can choose in drawing down federal funds. A state can choose an option that does not call for the exchange of interest. Second, the exchange of interest would be a valuable tool in promoting greater efficiency in cash management at the state and federal levels of government and in prompting the timely exchange of funds. Third, the interest exchange provision embraces the concept of "making whole," providing that whomever has the use of the money pays for it, thereby compensating the other party for any loss of investment opportunity. Fourth, the reciprocal interest exchange provision, as comprehended in supporting administrative regulations, would provide for a simplified approach to calculating interest, rather than the multiple calculation methods that federal agencies are currently imposing on states. We have taken steps to avoid program-by-program interest calculation. To help avoid any preoccupation with interest calculation, senior fiscal officers at the state and federal levels will deal with interest on a consolidated, statewide basis.

I am confident that the policies and procedures outlined in Section 4 of S. 1381 will result in a more efficient, effective and equitable intergovernmental exchange of funds. The procedures set out in the legislation have been tested by four states, and were fine-tuned through a rigorous dialogue between task force members.

At this point, I want to explain how some of the key concepts evolved. The State/Federal Cash Management Reform Task Force was established four years ago, largely in response to state and congressional concern over federal agency implementation of the delay of drawdown funding technique. Under the delay of drawdown technique, the state's drawdown is spread out over a number of days so that daily deposits will roughly coincide with the pattern in which checks have historically been presented to the bank for payment. The delay of drawdown technique was inconsistent with some state statutes and constitutions because states could not necessarily comply with the requirement that funds be on hand and available before checks were written.

But the delay of drawdown technique was not the only impetus for creating the task force. A number of studies, like the Grace Commission report, looked at financial transactions between the federal government and the states and found that some states were drawing down federal funds prematurely. In 1981 and 1982, the Joint Financial Management Improvement Programm (JFMIP) reviewed most of the financial transactions between the federal government and four states. During the same period, four additional states conducted self-evaluations using the JFMIP approach. These studies involving a combined total of eight states confirmed that, for some programs, states did draw down federal funds prematurely. These studies also found, however, that states were inadvertently being asked, for some programs, to use their own funds to support federally-assisted programs while awaiting the arrival of federal funds.

In an effort to provide for more uniformity and equity in intergovernmental finance, the Cash Management Task Force has been working to develop and test techniques for the equitable exchange of funds between the federal government and the states. In June 1983, the task force members signed a Memorandum of Understanding consisting of 17 policy statements governing intergovernmental financial transaction. Four states - Virginia, Indiana, Wisconsin and California - conducted pilot tests of techniques that had been set out in the MOU for exchanging funds. In general, the pilots improved the flow of funds between the federal government and the states involved. It is clear that progress among the pilot states was directly the result of cooperation between the participating states and the federal departments and agencies involved with the pilots. For example, many participating federal agencies have been very helpful in changing procedures that usually hinder the flow of cash to the states.

In a similar vein, pilot states worked diligently with their program agencies to make sure that cash was drawn down as close as possible to the time it was needed. The pilots demonstrated that, in a model situation, cash can be handled in an expeditious manner acceptable to both the federal government and the states.

A second MOU was signed by the task force in 1985. This new MOU restates support for the 1983 MOU, endorses the concepts in the bill before you, and presents administrative regulations and other guidance compiled by the task force. The new MOU is true to the task force's goal. It strives to assure that there are no winners and no losers when funds are transferred between the levels of government. Further, these documents seek to remedy a number of equity issues that were raised by states during the course of the pilot tests. While these equity issues were not technically part of the policies being tested by the four pilot states, it quickly became apparent that these issues, if unresolved, would continue to present serious problems in the flow of funds to the states. For the most part, these equity issues are dealt with in either the legislation and its interest exchange provision, the draft regulations developed by the task force, or in the associated guidance.

To a large extent, the equity issues identified by states deal with federal action or inaction that results in a state having to use its own funds to support federal programs. States, for instance, often have to use their own funds to help carry out a federal program because the federal agency disputes a claim or defers or disallows a state cost. Difficulties have also arisen when the federal government rescinds previously promised funding or denies funding for previously approved activities or costs.

In a slightly different vein, states also cited problems created by the inconsistent interpretation of federal regulations by federal employees. The interpretations may vary between the regional and national levels of the same agency, or may vary between federal agencies.

While some of these equity issues might be resolved by authorizing the federal government and the states to pay each other interest, others may require basic changes in federal program administration and management. For instance, more basic changes might be in order in the quarterly process some federal agencies use in awarding funds to states.

The quarterly award process becomes a particular issue when there is a delayed appropriation by Congress or an inadequate grant award by a federal agency. In these instances, a state may be forced to pay for a joint

state/federal program with its own funds. In response to state concerns with the award process, the task force agreed that the Department of Health and Human Services should test an annual grant award process in a number of states. It was hoped that this process will alleviate the red tape and potential funding shortfalls that states sometimes encounter on a quarterly basis.

Even if Congress appropriates funds on time and grant awards are adequate, the quarterly award process places significant demands on states because they must project future spending, report current spending, and reconcile previous spending each quarter. Through an annual process, it is hoped that these quarterly exercises would be reduce without any loss of meaningful federal budget control. States could not spend more that they now spend in a fiscal year, but they would be better prepared to cope with cycles in program spending.

Seven states are conducting pilot tests of the annual grant award process. These states - Tennessee, Indiana, Louisiana, Nebraska, Pennsylvania, Virginia and Wisconsin - are testing the process for programs administered by the Department of Health and Human Services (HHS). An independant assessment of them is being conducted by Deloitte, Haskins and Sells. If this assessment, and the experience of the parties involved, demonstrate that the annual grant award process streamlines grant administration and improves interaction between the federal government and the states, I would ask the subcommitte to request a briefing on the current HHS efforts to test the annual grant process, upon the completion of testing.

I also want to mention that much has already been done to apprise federal and state officials about the work of the task force. OMB and Treasury have been in touch with federal agencies on an ongoing basis, and state fiscal officials have been given periodic updates on the task force's efforts. In October 1986, NASACT, in cooperation with the U.S. Treasury Department and U.S. Office of Management and Budget conducted a seminar on the task force's policies, as reflected in S. 1381. Forty-five states were represented by the 280 people who attended the seminar. In addition, NASACT and the National Association of State Budget Officers in March 1987, adopted resolutions that support the work of the task force, and endorse the concepts contained in Section 4 of this bill.

With regard to the specific bill before you, there are three small amendments that I would like to propose. Since the bill was introduced there have been some developments that would make it expedient to clarify provisions dealing with the source of funds that can be used by the federal government in making interest payments to a state, and the application of the legislation to reimbursable construction grant programs. There has been some question as to whether interest due a state can come from funds appropriated for program purposes or out of the corpus of a trust fund, like the highway trust fund.

It is my feeling that these funds should not be used by the federal government to pay interest it owes the states, because this would penalize the states. In effect, interest owed to the states could possibly come from funds that were due to them for program purposes. I, therefore, ask that you accept amendments to clarify that interest paid to a state shall not be made from funds appropriated for program purposes or from the corpus of any trust funds authorized by federal statute, and that the crosscutting nature of the bill be modified to clearly incorporate reimbursable construction grant programs.

As I close, I would like to stress is that the task force developed its legislative proposal after years of discussion and compromise. One of the points receiving the greatest deal of attention was the provision in subsection (1) of section 6503 that requires the Secretary of the Treasury to consider costs incurred by a state in determining the amount of interest that must be paid by or that is owed to a state. It is important to consider that the policies set forth in S. 1381 are to improve government operations and modify and enhance the current cash management relationship between the federal government and the states. Because making these changes will improve efficiencies at both the state and federal levels of government, the task force determined that providing for the coverage of administrative costs by the Secretary of the Treasury was warranted.

In conclusion, I would hasten to add that this legislation can do much to build the level of confidence and trust that one level of government places in another, because it is based on a set of carefully scrutinized, tested and equitable principles. Further, it deserves special note that the unusual structure of the task force was conducive to success. The Task Force has been co-chaired by a federal representative and a state representative. Its members have included both state elected and appointed officials and senior federal officials. It has been staffed by both the U.S. Treasury and the National Association of State Auditors, Comptrollers and Treasurers. We have met at least quarterly and we have based our discussions on a mutually agreed-upon agenda. I am unaware of any other task force that has been structured or staffed in this way. It is a good approach. I recommend that it be used as a model for dealing with other intergovernmental issues.

Attachment to Testimony by Edward J. Mazur
July 22, 1987

Suggested Amendments to S. 1381

On Page 2, line 15, after the word "noncompliance." insert:

Such charges shall not be paid from funds appropriated for program purposes or from the corpus of any trust funds authorized by federal statute.

On Page 5, line 15, after the period "." insert:

No payments made under the provisions of this paragraph shall be made from funds appropriated for program purposes or from the corpus of any trust funds authorized by federal statute.

On Page 8, line 2, after the word "programs" insert:

, including the Federal-Aid Highway Programs and other reimbursable construction grant programs,

TESTIMONY BY

F. ARNOLD SCHULER
DEPUTY CONTROLLER, STATE OF CALIFORNIA
BEFORE THE
SUBCOMMITTEE ON GOVERNMENT EFFICIENCY, FEDERALISM
AND THE DISTRICT OF COLUMBIA
SENATE COMMITTEE ON GOVERNMENTAL AFFAIRS
ON
S. 1381
CASH MANAGEMENT IMPROVEMENTS ACT OF 1987

JULY 22, 1987

Mr. Chairman, I am Arnold Schuler, Deputy Controller of the State of California. Since 1983, I have been one of six State officials who have participated in the State/Federal Cash Management Reform Task Force which drafted the proposal that forms the basis of S. 1381.

Before beginning my comments on the legislation you are considering today, I would like to take this opportunity to thank you, Senator Roth, Senator Durenberger and the Governmental Affairs Committee for promoting and overseeing the work of our Task Force. Without your guidance and interest, I do not believe that this unprecedented cooperative effort between Federal and State officials to realize a more equitable cash management system would have ever materialized.

Since the instructions of the Committee to initiate this Task Force in late 1982, we have worked long and hard, sometimes disagreeing, but always with the utmost respect for our colleagues around the table. I believe it is because of this respect and the desire of all the participants to formulate a truly reasonable, workable and equitable package that we can come before you today to recommend the enactment of the major provisions of S. 1381, the Cash Management Improvement Act of 1987.

However, as we have found through our work over the past four years, Federal-State cash management policies encompass a wide and continually changing spectrum of programs and procedures which cannot easily be categorized and do not always fit a specific pattern. While we have tried to tackle these issues through an omnibus bill that will provide guidance for all Federal-State cash transfer programs, we recognize that specific instructions and regulations on the implementation of this measure will be the responsibility of the Department of Treasury, the Office of Management and Budget and the Federal departments and agencies which administer these programs.

Thus, with the full understanding that Administrations change and there will be different captains at the helm every four to eight years, we want to make every effort to ensure that the language in this legislation can stand the test of time and clearly reflects the goals outlined by the twelve Federal and State members of the Task Force, and hopefully, by this Committee.

I would, therefore, like to address several aspects of the legislation which I hope will be helpful to the Committee in formulating a final measure to present to the full Senate for its consideration.

The first is Section 3 of S. 1381 which provides authority to the Secretary of the Treasury to penalize Federal agencies which do not comply with Treasury's requirements that cash be disbursed to the States in a timely manner. Certainly, it is to the States' benefit that pressure be applied by Treasury on the Federal agencies to ensure that they are complying with the cash management procedures embodied in this legislation. However, the language does not specifically instruct Treasury on the source or the amount of the penalty. It is conceivable that Treasury could penalize a specific Federal agency for the exact amount of the interest paid a State as the result of poor Federal cash management practices and that such a penalty could be charged to program funds. Under such a scenario, the States and the program beneficiaries would be the ultimate losers with a reduced amount of program money left to be allocated to the States.

I believe that Treasury should have the flexibility to determine this penalty; however, charges against program funds would completely undermine the intent of this legislation to provide equity through interest exchange. Therefore, I would like to respectfully suggest that the Committee amend Section 3720B of this act by adding on line 15 after the word "noncompliance" the following:

> "Such charges shall not be paid from funds appropriated for program purposes or from the corpus of any trust funds authorized by Federal statute."

Such language would ensure that the program funds are left for their intended purpose and program beneficiaries would not be the victim of poor management at the Federal level.

The issue of the source of interest payments to the States has been one of longstanding concern to the State Task Force members. As mentioned earlier in my testimony, it is the very strong conviction of the State representatives that the integrity of program funds not be harmed by this proposal, and this conviction was shared by the majority of the Federal members of the Task Force.

In order to avoid any possible infringement on these funds, the original bill approved by all Task Force members, both Federal and State, called for the establishment of an Intergovernmental Interest Fund which would receive and disburse all interest exchange funds. Later, at the request of Treasury, the Intergovernmental Interest Fund was dropped in lieu of a provision contained in Section 6503, Paragraph (d) that authorized the Secretary of the Treasury to "pay, out of money in the Treasury not otherwise appropriated, such amounts as may be necessary for interest owed to a State under this subsection."

Although this initially appeared satisfactory, since the introduction of S. 1381, there have been some troubling representations by Treasury Department officials that it is their intent to ultimately charge these interest payments to program funds rather than Treasury funds not otherwise appropriated.

In specific, this representation was made to a meeting of State Highway Department officials in Nashville, Tennessee in early June. When these officials asked for the source of any interest payments to the States, the Treasury official replied that these funds would initially come from Treasury non-appropriated accounts, but ultimately, they would come from the highway trust fund.

As the Chairman knows, programs funded by the Highway Trust Fund are not entitlements and there are finite resources available for highway construction. Needless to say, these State highway officials wanted no part of any initiative that would shrink the size of the trust fund to pay interest which, in effect, would be penalizing the States, rather than the Federal government. I wholeheartedly concur, and I believe that I can speak for the other State members by saying that this is exactly the type of situation we were trying to avoid.

Therefore, I would once again respectfully request that the Committee consider an amendment to S. 1381 which I believe would clarify the intent of the legislation by ensuring that program funds are safe from use as Federal interest payments. At the end of Paragraph (d) of Section 6503, I recommend that the following language be inserted:

"No payments made under the provisions of this paragraph shall be made from funds appropriated for program purposes or from the corpus of any trust funds authorized by Federal statute."

This language should clarify any misconceptions that the Federal interest payments to the States may be derived from program funds.

In addition, to ensure that there is no confusion regarding the inclusion of all Federal-State cash transfer programs under the provisions of this Act, I also suggest that S. 1381 be amended by inserting the following on Page 8, line 2 after the word "program":

", including the Federal-Aid Highway Program and other reimbursable construction grant programs,"

Another area I would like to address is the importance to the States of recovering the costs of administering the interest exchange program. This has been a critical issue to the States since the inception of the Task Force in 1983. Its importance was embodied in the initial Memorandum of Understanding signed in June, 1983 by all Task Force Members which instructed the pilot tests to "Determine equitable methods for providing administrative and start-up costs attributable to the specific cash management practices being implemented..."

Let me first explain the interest exchange program. This program involves the tracking of Federal and State funds utilized on Federal assistance programs to determine whether either the State or Federal governments benefited financially from the flow and use of the other's funds. In those cases, where one of the parties benefited, interest is owed to the other. The overall objective of the program is to promote the most efficient use of Federal and State funds relative to Federal assistance programs.

Both the Federal and State representatives to the task force believe that the interest exchange program is needed to promote and highlight the efficient use of funds. In fact, during the pilot tests conducted in four States, the proposed health and human services "annual grant award" process was discovered. This process is expected to smooth the flow of funds for Federal assistance program purposes as well as save significant paperwork between the State and Federal governments. We would expect the identification of similar cash management improvements as the States administer the interest exchange programs.

The pilot tests conducted in four States identified the need for well structured state systems to identify the nature and flow of funds. Some of these systems can utilize existing state fiscal processes (Wisconsin) while others must be constructed from scratch (California). In all pilot States, the greatest problem and complexities were involved in tracking exceptions which were outside the reaches of existing processes.

The Department of Treasury has emphasized that "simplistic" approaches can be used for calculating interest as well as tracking over 90 percent of Federal funds contained in the top 10 to 15 Federal assistance programs. The States agree that many of the funds can be tracked using basic approaches. However, as the pilot confirmed, the remaining exception portion of the costs are quite difficult to track and add significantly to the cost of data collection.

The pilot program identified the nature and extent of costs involved to start up and operate the pilot interest exchange programs. These costs range from $7,500 to $43,000. The pilot clearly demonstrated that additional costs would be incurred by all States in operating this program; however, it is unlikely that significant amounts will be required to be paid by the Treasury. For most, the cost of administration will be netted out of interest owed to the Federal government. However, in those cases where the Federal government owes the States interest, such costs will involve a direct payment to the States.

We believe that because the burden of all record-keeping is on the States, such compensation is consistent with the Memorandum of Understanding signed by all Federal and State Task Force members which cites that neither the Federal nor State governments should benefit or suffer financially as a result of the transfer of cash in support of Federal assistance programs. Additionally, the State of California qualified its signature on the 1985 Memorandum of Understanding upon the agreement that administrative costs would be paid to the States for the administration of the reciprocal interest programs.

Based upon this policy, we believe that the Federal government should be responsible for any administrative expense incurred in managing the reciprocal interest programs. Such reimbursement is consistent with Federal payments for other services provided by the States to the Federal government.

Therefore, it is very important to the States that Paragraph (1) of S. 1381 be retained or even strengthened

to ensure that the States are fairly reimbursed for their investment and the time and cost incurred in the administration of this system.

In closing, Mr. Chairman, I want to once again thank you for your commitment to improving fiscal relationships between the Federal and State governments. I believe I can speak for all the State members of the Task Force in saying that we look forward to working with you and the Committee in resolving any technical or philosophical difficulties with this measure and securing its Senate passage as quickly as possible.

Testimony By

Beverly Balakhovsky

Chief Accountant, State of Wisconsin

Before The

Subcommittee on Government Efficiency, Federalism and the District of Columbia

Senate committee on Governmental Affairs

on

S.1381
Cash Management Improvements Act of 1987

July 22, 1987

Mr. Chairman, I am Beverly Balakhovsky, Chief Accountant of the State of Wisconsin. I want to thank you for giving me the opportunity to address you this morning on S.1381, Cash Management Improvements Act of 1987.

As a member of the Task Force I want to not only concur but to endorse the comments made by Mr. Mazur and by Mr. Schuler.

The concepts embodied in S. 1381 were very carefully negotiated and crafted by the state and federal members of the Task Force to ensure that there are no winners and no losers in the exchange of funds between the federal government and the states. This bill provides the framework to achieve equity for both levels of government and the immediate beneficiaries of this equity are the taxpayers. As Mr. Mazur has discussed, interest is one aspect the bill provides to ensure equity. But interest also achieves other important benefits. It provides a quantitative basis for indicating and identifying problems and inefficiencies at both the state and federal levels. Resolution of problems and increased efficiency has been accomplished in the context of the pilots. The Task Force has clearly demonstrated that resolving problems and improving efficiency is not only possible, but that it may be one of the most effective ways to ultimately achieve cash management improvements in the federal and the state governments.

During the initial pilots it became very clear that there were specific inequities to the states that would be better resolved by attempting to change the factors that caused the problems than by calculating interest associated with the inequities. One of these problems deals specifically with the quarterly grant award process for state administered federal entitlement programs. The major entitlement programs are Medicaid and Aid to Families with Dependent Children. The quarterly grant award process causes a number of difficulties for states. It interrupts the state's access to needed federal cash and forces the state to use its own funds to support the program while awaiting the next quarterly grant award and/or the approval and processing of a supplemental award. This temporary use of state monies reduces the state's investment opportunities on its own monies, thereby, in effect, causing the state to subsidize the federal program in ways that were never intended by Congress. The quarterly award process results in an excessive amount of paperwork at both the state and federal level that is unnecessary. The quarterly award process does not improve the accountability at either the state or the federal level, but in fact gives a false sense of security about accountability.

In response to the issues raised by the quarterly award process, the Task Force agreed that the Department of Health and Human Services should test an annual grant award process in a number of states. It is important to note that the Annual Grant Award process does not allow the states to draw their money all at one time, but in fact requires a state to time its cash drawdown to meet actual, allowable program expenditures as they are made by the state. The purposes of the pilot as described in the Memorandum of Understanding between each participating state and the department are to: reduce the paperwork requirements and administrative costs associated with quarterly awards; minimize periodic interruption in state access to needed federal cash for state administered federal programs; help achieve comprehensive equity in the federal/state cashflow; and improve the present level of accountability over and confidence in the timing of drawdowns from the U.S. Treasury. The pilot tests cover the period from October 1, 1986 to September 30, 1987 are are being conducted in seven states, Wisconsin, Tennessee, Indiana, Louisiana, Nebraska Pennsylvania and Virginia.

I would especially like to thank you Mr. Chairman, for your assistance in the initiation of the Annual Grant Award pilot. The Office of Management and Budget expressed opposition to this project. However, through the assistance of you and your staff and several other members of Congress the objections were overcome and the project was allowed to begin.

Even though the pilots are not yet completed, there are some preliminary results that I would like to share with you. The annual grant award process has: significantly reduced the number of grant awards which reduces administrative and paperwork burdens substantially at both the federal and state level; reduces the number of times the state's access to federal cash is interrupted, thereby saving the state of Wisconsin over $250,000 in potentially lost investment earnings on state funds used for federal programs; demonstrated that equity can be achieved in a cooperative State/Federal venture; and clearly shown that effective management, oversight and monitoring of the annual grant process results in improved state and federal systems, procedures and internal and external controls, increased efficiency at both levels of government and improved identification and resolution of problems in a timely manner. To date the pilot has demonstrated that there are significant benefits for both the federal government and state government. These benefits are in increased efficiency, improved controls and systems, more effective use of scarce staff resources, and significantly improved cash management at both the state and federal level of government.

Based on these preliminary results I would recommend that the seven pilot states continue the annual grant award process as spelled out in the Memorandum of Understanding which calls for their continuation as the pilot states select and begin the implementation of cash management improvements as embodied in S.1381. The Department of Health and Human Services will be issuing a report on the results of the Annual Grant Award in early 1988. I respectfully encourage the subcommittee to closely examine this report in light of the benefits that I believe will result for both the federal and state governments. Should the report demonstrate that the Annual Grant Award program is a positive step toward equitable cash management, the state members of the Task Force may once again request the subcommittee's assistance in extending the program to all the states as they individually select and implement the concepts of improved cash management as embodied in S.1381.

In closing, Mr. Chairman, I want to again thank you for giving me this opportunity to comment on the importance of S.1381 and the annual grant award as being critical and effective mechanisms to assure equity and to effect necessary cash management improvements at the state and the federal level which will ultimately benefit the taxpayer in more efficient government at all levels.

National Association of
State Auditors, Comptrollers and Treasurers

PRESIDENT
Roland W. Burris
Comptroller
201 State House
Springfield, Illinois 62706
(217) 782-6000

December 12, 1986

Mr. Joseph R. Wright, Jr.
Deputy Director
Office of Management and Budget
Old Executive Office Building
Washington, D.C. 20503

Dear Mr. Wright:

As Co-Chairman of the Joint State/Federal Cash Management Reform Task Force, I am writing to express the concern of the State members with OMB's proposed changes in the Intergovernmental Financing Act of 1986, which was forwarded to the Congress in August, 1986.

During a meeting of the Task Force in October, 1986, these proposed amendments were discussed at length with OMB's representatives on the Task Force, Palmer Marcantonio, Acting Deputy Associate Director for Financial Management, and Betty Bradshaw, Budget Methods Analyst. Since both of these officials are new members of the Task Force, they were not involved in the direct discussions within OMB on the proposed changes in the bill. At their recommendation, we are writing to you to request a review of these changes, and we are also asking for an Administration endorsement of the original legislation adopted by the Task Force and approved by the Senate Committee on Governmental Affairs.

As you know, the Intergovernmental Financing Act was drafted by the Cash Management Reform Task Force after months of tedious review, indepth discussions and extended negotiations between the State and Federal members. The Task Force includes representatives from six States, two representatives from OMB and one each from the Departments of Treasury and Health and Human Services, the Environmental Protection Agency, and the Joint Financial Management Improvement Project. In addition, sessions were often

First Vice President: Joan Finney, State Treasurer, Kansas; *Second Vice President:* Thomas Hayes, Auditor General, California; *Treasurer:* Earle E. Morris, Jr., Comptroller General, South Carolina; *Secretary:* Mary Ellen Withrow, State Treasurer, Ohio; *Immediate Past President:* Anthony Piccirilli, Auditor General, Rhode Island

SECRETARIAT: Reimond P. Van Daniker, Executive Director for NASACT, The Council of State Governments Iron Works Pike, P.O. Box 11910, Lexington, KY 40578, Telephone (606) 252-2291, and 444 N. Capitol Street, Washington, DC 20001, Telephone (202) 624-5460

attended by representatives from other Federal agencies, specifically the Department of Transportation, and other States, and the input of all of these officials was considered in the drafting of the text.

The final legislative proposal was adopted by all State and Federal members of the Task Force in a Memorandum of Understanding dated November 1, 1985. This legislation came to the attention of the Senate Committee on Governmental Affairs, and with some minor adjustments, the legislation was included in Title IV of S. 2230, the Federal Management Reorganization and Cost Control Act of 1986, which was favorably reported by the Committee on July 31, 1986.

The State members of the Task Force are committed to the passage of legislation that will create an equitable environment for the transfer of cash between the Federal and State governments. It is in this spirit that the National Association of State Auditors, Comptroller and Treasurers, in cooperation with OMB and Treasury, hosted a seminar in October to educate State and Federal officials in the work of the Task Force and to ask for their cooperation and support in making these proposals a reality.

I have given this lengthy background in order to emphasize the importance we attribute to maintaining the language included in the original legislation approved by the Task Force and the Senate Governmental Affairs Committee. Last year, we were told by Senate officials that for this measure to pass, it needs bipartisan support from the Administration and the States. Now, with the change in Senate leadership, this unanimous support is even more critical. However, the State members of the Task Force cannot lend their support to OMB's version of the legislation because it contains substantial and fundamental differences from the original measure approved by the Task Force. These differences include the following:

Section 4(c) and 4(e). The OMB draft requires States to calculate interest owed to the Federal government at the 13-week Treasury bill rate or at the rate earned by the State, whichever is higher, as determined by the Secretary. While the 13-week Treasury rate was endorsed by the Task Force, language requiring the calculation at the rate earned by the State, if higher, was not contemplated. Such a calculation would considerably complicate the administration of the interest provisions for the States, requiring adoption of a complex methodology and a detailed tracking system for

determining which interest rate would be used. It would most certainly weaken support for the entire proposal among a number of State officials who are leery at best of the interest provisions.

In addition, the equity of the Task Force agreement is significantly undermined because the Federal government would be required to pay interest to the States at the Treasury bill rate or the rate earned by the State, whichever is lower. Clearly, such a provision cannot be acceptable to the States. Once again, the 13 week Treasury rate was adopted by Task Force representatives from Treasury and OMB after considerable thought and discussion over the merits of this approach.

Section 4(d). OMB's draft takes an approach for payment of interest to the States which was discussed and dismissed by the Task Force. Your draft proposes that Federal agencies reimburse the Treasury for interest payments out of "any appropriations available to carryout the grant program involved." It was not the intent of the task force to penalize grant recipients by reducing grant funds available for program purposes, but instead to require the interest payments be made from a central fund maintained by the Treasury.

Section 4(e). Although Section 4(e) was discussed above in conjunction with Section 4(c), there is another change in this section which is unacceptable to the States. The OMB draft states that:

> "If a State is required by law or regulation to disburse its own funds at a time and for purposes for which the Federal Government is obligated to provide Federal funds under Federal law, regulation, or Federal-State agreement, the State shall be entitled to interest..."

It is particularly disappointing to the States that the OMB draft modified the agreed-upon language in this manner. The language included in the Task Force recommendation was painstakingly worked out so that it would conform to the spirit of the interest transfer provisions. The Task Force language states:

> "If a state disburses its own funds for program purposes in accordance with Federal law, regulation, or Federal-State agreement..."

All the Federal and State members of the Task Force acknowledge that in most, and perhaps all, cases, the State

governments are not actually required to spend their own funds when Federal funds are not available. However, State governments cannot politically or realistically turn program funds on and off like a spigot. It is in the national interest that such programs as Aid to Families with Dependent Children and Medicaid run smoothly and continuously, even if Federal funds are not received on time. Therefore, it is impractical for States to stop programs due to the failure of Federal agencies to forward funds in a timely manner. However, technically, if the term "required" is used, States would never be entitled to interest on funds. Thus, the phrase "in accordance with" was adopted so that it would be clear that if a State were acting in good faith by conducting existing programs that it would be entitled to interest. This language was discussed with the Senate Governmental Affairs Committee and was acceptable to its Members.

Section 4(f). OMB's draft requires States to pay interest on credits or refunds. The Task Force legislation provides that interest on refunds should be considered when setting overall interest obligations between the State and the Federal government. Such an offset reduces the administrative burden on the States and contributes to the fundamental objective of the Task Force that interest should be offset as much as possible between the parties.

Section 4(l). The OMB draft provides that amounts paid to a State from the Department of Treasury's Claims, Judgements and Relief Account will be subject to interest payments only after final judgment is rendered requiring the payment of interest. This provision could be unfair to the States if it took an inordinate amount of time for final judgment to be rendered on a particular case. Further, in cases involving appeals or litigation, it is unclear at what point the States would owe interest to the Federal government.

During the lengthy Task Force discussions on interest payments, the Department of Treasury, the subject agency, never proffered this provision as a possible part of the bill. Since this provision was never discussed by the Task Force, and therefore, has not had the scrutiny of the other sections, we believe it should be deleted from your draft at this time subject to further review by the Task Force.

Additionally, Section 4(l) as approved by the Task Force and adopted by the Governmental Affairs Committee as part of S. 2230 contained a very important provision that was deleted in the OMB draft. This section provided that,

in determining the amount to be paid by the State to the Federal government or to a State by the Federal government, the Secretary shall consider costs incurred by the State in determining the amount due.

Administrative cost reimbursement was the subject of lengthy debate and review since the inception of the Task Force, and the relatively moderate language that was finally included in the Task Force bill was a compromise by the State members who actually preferred that administrative costs be specifically reimbursed. The omission of this compromise language is a serious breach in the Task Force agreement and is unacceptable to the States.

The State members of the Task Force believe that the changes proposed by OMB will jeopardize State support for the Intergovernmental Financing Act and could seriously undermine the chance of passage of this measure. We hope that OMB will agree to modify its proposal to conform with the intergovernmental financing provisions of S. 2230. Such an act would give encouragement to the States that the product of our three year joint effort is supported by the Administration.

With the change in OMB Task Force representation during this critical review period, we recognize that all the background and views of the States may not have been fully explained to key OMB officials. Therefore, we wanted to take this opportunity to explain our concerns to you and request that the OMB draft be modified accordingly prior to its resubmission in the 100th Congress.

The State members of the Task Force will be happy to meet with you or your representatives at any time to discuss these matters in more detail. We look forward to working with you toward the implementation of a cash management system in which we can all be proud. We believe that such a goal can be accomplished if the original legislation drafted by the Task Force is submitted to the Congress and supported by the States and the Administration.

Sincerely,

Edward J. Mazur, Co-Chairman
Joint State/Federal Cash
Management Reform Task Force

cc: State and Federal Members
Cash Management Reform Task Force

MEMORANDUM OF UNDERSTANDING
FOR FINANCING FEDERAL ASSISTANCE PROGRAMS

This is to confirm agreements reached by the Joint State/ Federal Cash Management Reform Task Force. The agreements include the attached cash management policies and are intended to achieve an equitable system of intergovernmental cash management.

We agree to work toward acceptance by and implementation of these policies in the State and Federal Governments. This includes:

- Pursuing resolutions at meetings of major State groups (i.e., NASBO and NASACT) endorsing the cash management policies;
- Initiating the necessary changes to implement the policies in the Federal agencies; and
- Undertaking, as soon as possible, pilot tests of the various funding alternatives provided by the policies, involving an appropriate number of States, Federal agencies, and programs.

It is agreed that the pilot tests will:

- Begin as soon as possible and last no more than six months, and will include an appropriate number of Federal programs;
- Examine the viability of the various proposed funding options, including:
  - Checks paid letter of credit.
  - Estimated checks cleared letter of credit (Delay of Draw).
  - Checks issued letter of credit with interest paid or credited (using, for example, the Separate Bank Account or Day of Disbursement method).
- Determine equitable methods for providing for administrative and start-up costs attributable to the specific cash management practices being implemented; and
- Serve as the first test of actual implementation of the proposed policies in the State and Federal Governments.

It is understood that States currently on the Delay of Draw method will continue using this method until they implement one of the funding methods provided for by the attached cash management policies. It is understood that Federal agencies will not proceed to expand use of the Delay of Draw method unless requested by a State.

If the results of the pilot tests are mutually satisfactory, it is further understood that the individual States will decide on and begin implementing a funding method, or methods, as soon as possible after the conclusion of the pilot tests.

John F. Rogan (Wisconsin)
State Finance Director

James F. Kelly
Deputy Associate Director,
Management Reform
Office of Management & Budget

Richard Standiford
(New Jersey)
Deputy Director, Division
of Budget and Accounting

John J. Jordan
Deputy Associate Director,
Finance and Accounting
Office of Management & Budget

Edward A. Mazur (Virginia)
Comptroller
Department of Accounts

William M. Henderson
Director, Cash Management
Office of Management & Budget

Julian Ridlen (Indiana)
State Treasurer

Russell Morris
Assistant Commissioner
Banking and Cash Management
Department of the Treasury

F. Arnold Scnuler
(California)
Deputy State Controller

David V. Dukes
Deputy Assistant Secretary,
Finance
Department of Health and
Human Services

Attachment

Intergovernmental Cash Management Policies for Financing Federal Assistance Programs

1. There shall be a set of Government-wide cash management policies and practices that govern all exchanges of funds between Federal and State Governments.

2. Intergovernmental cash management practices should be such that neither the Federal nor State Governments benefit financially or suffer financially as a result of the transfer of cash in support of Federal assistance programs.

3. It is understood that the Federal Government is entitled to earnings on cash provided by the Federal Government to a State government prior to the time such cash is needed to redeem a warrant, a check, or payment by other means. It is also understood that a State government is entitled to earnings on cash advanced by such State government to redeem a warrant, a check, or payment by other means, prior to reimbursement by the Federal Government on programs for which Federal payment is required.

4. The Federal Government shall make grant allocations and awards in such a manner and in such amounts to assure that funds are adequate to meet State cash disbursement issuance requirements.

5. States shall bill based on actual cash disbursement needs or a close approximation of expected cash disbursement needs (plus the allowance for depreciation, amortization, and overhead costs, as approved in accordance with OMB Circular A-87).

6. Due to the variety of constitutional, statutory, and administrative restrictions existing among the 50 States, several techniques for transferring cash between Federal agencies and State governments shall be made available for selection by each State. These techniques are:

a. Checks paid letter of credit.

b. Estimated checks cleared letter of credit (Delay of Draw).

c. Checks issued letter of credit with interest paid or credited (using, for example, the Separate Bank Account or Day of Disbursement method).

7. States selecting the checks issued letter of credit with interest paid or credited option shall:

- Draw down Federal funds as close as possible to the time of issuance of warrants, checks, or payments by other means.

- Pay or credit the U.S. Treasury interest on the balance of Federal cash in banks/State treasuries based on the Federal funds rate; the specific rate and method to be determined.

8. Since the checks issued letter of credit with interest paid or credited option is new, there should first be a pilot test in three or four States in order to resolve any initial procedural or operational matters that may arise.

9. The Federal Government is willing to work with the States and State organizations to consider other financing systems or methods proposed by the States as long-range or future alternatives.

10. The Federal Government shall pay to or credit the appropriate State Treasury interest on the balance of ___ State cash advanced on Federal programs based on the Federal funds rate; the specific method and rate to be determined.

11. Whenever feasible, each State and the concerned Federal agencies shall implement a single cash management technique for all Federal programs in which the State is participating.

12. Federal agencies and each State government will move as quickly as possible to adopt the technique(s) chosen by each State.

13. All transfers of funds between the States and the Federal Government shall be accomplished by wire transfer to ensure quick delivery of funds.

14. Where Federal statutes require reimbursement, the Federal Government shall revise regulations or administrative procedures to ensure that cash is transferred as closely as possible to the time that States make disbursements.

15. States will apply sound businesslike practices when disbursing Federal funds to secondary recipients and contractors, and not disburse or handle such cash at a faster rate or in a different manner than it handles its own cash.

16. For Supplemental Security Income State supplement payments, the same cash management principles shall be followed, except the State will be considered the disbursing agent and the Federal Government the payee.

17. Each State will designate a specific State official(s) (name and title) with the statutory or administrative authority to coordinate all State agencies to review, approve, and/or enter into an agreement with the U.S. Government for the purpose of implementing these cash management policies.

CHECKS PAID LETTER OF CREDIT

DESCRIPTION

Grantee is provided an irrevocable letter of credit to establish a separate zero-balance bank account in a commercial bank. Grantee issues warrants or checks for program purposes against the account, which are processed according to normal banking procedures.

At a predetermined time each day, the commercial bank totals the checks presented against the zero-balance account that day; telephones the district Federal Reserve or branch; and relays the name of the grantee for which it is drawing funds, the letter of credit number, and the amount of Federal funds needed that day. The Federal Reserve Bank verifies and obtains approval for the request. It then credits the commercial bank's reserve account the same day with a book entry, which in effect transfers the funds from its reserve account to the grantee's account. This enables the grantee to maintain the account with a zero balance at the end of each bank day.

The commercial bank normally requires a compensatory balance or payment of fees for handling the zero balance account.

ESTIMATED CHECKS CLEARED LETTER OF CREDIT SYSTEM
(DELAY OF DRAW)

DESCRIPTION

The State is provided a letter of credit which is irrevocable to the extent the State has obligated funds in good faith and in accordance with the grant, contract, or other agreement for the execution of an authorized Federal program. A copy of the letter of credit is also given to the U.S. Treasury, authorizing the U.S. Treasury to make payments to the State upon demand from operating accounts maintained by the U.S. Treasury at the Federal Reserve Bank, subject to dollar limits indicated on the letter of credit.

The State issues checks or warrants for program purposes against its operating account. The checks or warrants are processed according to normal banking procedures. Using historical warrant/check clearance patterns, the State requests its commercial bank, as often as daily, to initiate a request for funds to cover the checks or warrants it expects will be presented for payment the next business day.

The bank sends a message by wire to Treasury indicating the name of the State, the amount requested, and the letter of credit number. The Treasury and the program agency review and verify the request for funds. Within 24 hours of the request, the Treasury wire transfers immediately available funds to the commercial bank for credit to the account of the State.

CHECKS ISSUED LETTER OF CREDIT SYSTEM
WITH INTEREST PAID OR CREDITED (SEPARATE BANK ACCOUNT)

DESCRIPTION

State is provided a letter of credit which is irrevocable to the extent the State has obligated funds in good faith and in accordance with the grant, contract, or other agreement for the execution of an authorized Federal program. A copy of the letter of credit is also given to the U.S. Treasury, authorizing the U.S. Treasury to make payments to the State upon demand from operating accounts maintained by the U.S. Treasury at the Federal Reserve Bank, subject to dollar limits indicated on the letter of credit.

The State instructs its bank, as often as daily, to initiate a request for funds immediately preceding the issuance of warrants or checks for program purposes. The bank sends a message by wire to Treasury stating the name of the State, the amount requested, and the letter of credit number. The Treasury and the program agency review and verify the request for funds. Within 24 hours of the request, the Treasury wire transfers immediately available funds to the commercial bank for credit to the account designated by the State. Interest is credited to the Federal Government by the bank monthly on the average daily balance in the account at the Federal funds rate.

When Federal/State matching funds are involved, there are a number of options available for consideration:

1. State may issue checks/warrants directly against the separate account for only the Federal share of program costs.

2. State may issue checks/warrants directly against the separate account for both the Federal and State shares, provided that the State transfers the State share to the separate account on the same day the checks/warrants are presented to the account for payment.

3. State may issue checks/warrants against its own account for both the Federal and State shares and transfer the Federal share to the State account on the same day the checks/warrants are presented to the account for payment.

4. State may issue checks/warrants against either the State or Federal account up to that percentage of the total value of warrants which corresponds to the State or Federal matching percentage share for a program. For example, if a State issued a total of $300 in warrants for a program in which the Federal Government paid 90% of the costs with the State matching 10%, the State could then issue warrants totaling $270 against the Federal account and $30 against the State account.

CHECKS ISSUED LETTER OF CREDIT
WITH INTEREST PAID OR CREDITED (DAY OF DISBURSEMENT)
(BY STATE)

DESCRIPTION

The State would be provided a letter of credit which is irrevocable to the extent that the State has obligated funds in good faith and in accordance with the grant, contract, or other agreement for the execution of an authorized Federal program. A copy of the letter of credit is also given to the U.S. Treasury, authorizing the U.S. Treasury to make payments to the State upon demand from operating accounts maintained by the U.S. Treasury at the Federal Reserve Bank, subject to dollar limits indicated on the letter of credit.

On the day of disbursement, rather than either before or after the fact, the State would request the transfer of funds into any bank/State treasury account it might designate. The day of disbursement is defined as the day that is as close as possible to the time needed by the State for the issuance of warrants, checks, or payments by other means.

Under the "day of disbursement - by State" method, the State would pay or credit the U.S. Treasury with interest on Federal funds held in the State bank/State treasury accounts for a negotiated average number of days, representing the average number of days from the day funds were received in the State's bank/State treasury account until the day that cash was required to redeem the State's warrant, check, or payment by other means.

Interest would be calculated annually, based on the total value of Federal funds during the State's entire fiscal year, multiplied by the above predetermined and negotiated average number of days that the cash was held, times a predetermined and agreed-upon interest rate, less a reasonable administrative charge. The number of days used would, in part, be calculated using a predetermined and agreed-upon check clearance pattern and would assume that specific percentages of disbursements cleared the bank each day subsequent to the issuance of warrants, checks, or payments by other means.

Under the "day of disbursement - by State" method, the comparable interest costs to the State on Federally sponsored programs, where State funds must be disbursed prior to the receipt of Federal funds or where the Federal Government administers a joint Federal/State program, would be calculated and netted against any interest amounts owed to the Federal Government. The net interest due to or owed by the Federal Government would be transmitted or billed to them on a predetermined frequency, preferably annually, after the close of the State's fiscal year.

It should be noted that the desirability of this method stems from the facts that: (a) check clearance patterns are determined on a basis that has already been determined to be acceptable by the Federal Government; (b) one set of check clearance patterns may be developed for the entire State, thereby enabling existing systems and procedures to continue; (c) interest rates would be obtained from some readily available published source, and therefore should result in a non-complex methodology for their application; and (d) Federal and State Government activity would be subject to audit by both State and Federal auditors and could include sanctions to encourage compliance.

Since the objective of considering various Federal/State cash management alternatives is to achieve equity with regard to the use of Federal and State funds, all predetermined items, including check clearance patterns and interest rates, would be subject to annual renegotiation. These items, together with the State's actual performance in drawing down Federal funds or the Federal Government's performance in remitting payments after State funds have been expended or its performance in expending State funds which the Federal Government administers, would be subject to periodic audit and compliance testing.

A MEMORANDUM OF UNDERSTANDING

Regarding Proposed Amendments to the

Intergovernmental Cooperation Act

and

Supporting Administrative Regulations That Will,

in Combination, Create Appropriate Equity

in the

Transfer of Funds Between the

Federal Government and the States

Entered into By The Members of

The State/Federal Cash Management Reform Task Force

in Washington, D.C.

on November 1, 1985

A MEMORANDUM OF UNDERSTANDING

Regarding Proposed Amendments to the
Intergovernmental Cooperation Act
and
Supporting Administrative Regulations That Will,
in Combination, Create Appropriate Equity
in the
Transfer of Funds Between the
Federal Government and the States

Entered into By The Members of
The State/Federal Cash Management Reform Task Force
in Washington, D.C.
on November 1, 1985

The members of the State/Federal Cash Management Reform Task Force, meeting in Washington, DC on November 1, 1985, wish to formally establish their joint and mutual agreement as to the manner in which the Intergovernmental Cooperation Act and supporting administrative regulations may best be amended and established to bring about appropriate equity in the transfer of funds between the Federal Government and the States. This agreement is represented by and presented in the following documents, dated November 1, 1985, that are an integral part of this Memorandum of Understanding.

1. Amendments to Title 31, U.S.C. - the "Intergovernmental Financing Act of 1986," an act to amend the Intergovernmental Cooperation Act by improving the method of disbursing Federal grant money, and for other purposes.

2. Amendments to 31 CFR Part 205, Department of the Treasury Fiscal Service Regulations, regarding payments between the Federal Government and recipient organizations.

3. A revised draft of Circular A-102 "uniform requirements for grants to States and local governments," which contains sections directly concerning cash management practices between the Federal Government and the States and sections addressing the management and awarding of grant funds.

Further, this agreement is additionally represented by proposed sections of the Treasury Financial Manual that concern cash management practices between the Federal Government and the States and other requirements necessary to support the implementa-

tion of the proposed Intergovernmental Financing Act of 1986. These proposed sections of the Treasury Financial Manual will be available at a later date following further review by the Task Force.

In arriving at the terms of this Memorandum of Understanding, the members of the Task Force had hoped to be able to include a requirement that all Federal program agencies embrace the concept of making annual grant awards, which the States believe would mitigate against undue delays in funding that are occasionally associated with quarterly grant award procedures. The Task Force was unable to complete testing of such annual awards procedures, and, not wanting to delay further the issuance of this MOU, chose to postpone a recommendation concerning the establishment of a specific requirement for annual grant awards, at this time. The Task Force looks, however, with much interest on the current efforts of the Department of Health and Human Services, in cooperation with the Office of Management and Budget, in planning for and scheduling to begin in the near future pilot tests of annual grant procedures in several States.

In entering into this Memorandum of Understanding, the State/Federal Cash Management Reform Task Force brings to completion, in all essential aspects, the second phase of its work. This second phase involved the completion of pilot testing called for in the Memorandum of Understanding of the Task Force, dated June 1983, and the development and issuance of proposed implementing legislation and regulations. Further, in entering into this Memorandum of Understanding, the members of the Task Force wish to express their continued confidence in the policies and principles set forth in the June 1983 Memorandum of Understanding and to provide their reasonable assurance that these policies and principles have been tested in substantial measure in the field and have been found to be effective and operative in ensuring appropriate equity in the transfer of funds between the Federal Government and the States. Most especially, the members of the Task Force have concluded that the attached proposed legislation and supporting regulations, and the sections of the Treasury Financial Manual, noted above, together constitute the following:

1. A set of government-wide cash management policies and practices that can govern exchanges of funds between the Federal and State Governments, and

2. Intergovernmental cash management practices which assume that neither the Federal nor State Government benefit financially or suffer financially as a result of the transfer of cash in support of Federal assistance programs.

In arriving at this Memorandum of Understanding of November 1, 1985, the members of the State/Federal Cash Management Reform Task Force are confident that their efforts, since entering into the June 1983 MOU, have been constant, diligent, rigorous, professional in approach, and objective in their setting. Further, the members of the Task Force believe that the contents of the attached proposed legislation and supporting administrative regulations represent the clear attainment of a substantive and very reasonable level of consensus among all members of the Task Force and represent a fairly derived accommodation of the various views and positions of individual members of the Task Force.

The members of the State/Federal Cash Management Reform Task Force earnestly hope that the Administration, the Congress, the States, and other interested parties will find use in and benefit from this Memorandum of Understanding of November 1, 1985, entered into by:

Edward J. Mazur, Co-Chairman
Comptroller
State of Virginia

John J. Lordan, Co-Chairman
Deputy Associate Director,
Financial Management
Office of Management and Budget

Bill Gunter
State Treasurer
Florida

David V. Dukes
Executive Director
Joint Financial Management
Improvement Project

Lewis E. Harris
Assistant Commissioner
for Administration
Tennessee Department of
Human Services

William M. Henderson, Director 11/14/85
Resource Management Division
Office of Comptroller
Environmental Protection Agency

Julian L. Ridlen
Treasurer of State
Indiana

Henry G. Kirschenmann, Jr.
Deputy Assistant Secretary
Procurement, Assistance and
Logistics - Department of Health
and Human Services

F. Arnold Schuler 1-2-86
Deputy State Controller
California

John W. Merck
Deputy Associate Director
Planning and Communications
Management
OMB

Richard B. Standiford 11/8/85
Director, Division of
Budget and Accounting
New Jersey

Russell D. Morris 11/1/85
Assistant Commissioner
Federal Finance
Financial Management Services
Department of the Treasury

To amend Title 31, United States Code, to improve the method of disbursing Federal grant money, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

Section 1. This Act may be cited as the Intergovernmental Financing Act of 1986.

Section 2. Purpose. The purposes of this Act are to:

(a) Establish general guidelines within which the Secretary of the Treasury will develop regulations concerning all transfers of funds between the Federal Government and the States, consistent with the Memorandum of Understanding agreed to by the Joint State/Federal Cash Management Reform Task Force in 1983.

(b) Assure that the States and the Federal Government accord each other the same equitable treatment with regard to the timing and manner of transfers and the management of funds.

(c) Establish general guidelines within which the Executive Departments and Agencies, in cooperation with the States, will develop regulations concerning the timely awarding of grants to the states.

Section 3. Section 6501 of Title 31, United States Code, is amended by renumbering Subsections (7), (8), and (9) as (8), (9), and (10), respectively, and by adding the following new subsection:

(7) "Secretary" means the Secretary of the Treasury.

Subsection (8) is amended to read as follows:

(8) "State" means a State of the United States, the District of Columbia, a territory or possession of the United States, and an agency, instrumentality, or fiscal agent of a State but does not mean a local government of a State.

Section 4. Section 6503 of Title 31, United States Code, is amended to read as follows:

(a) Consistent with program purposes, and regulations of the Secretary, and by means mutually agreed upon by the Secretary and the State, the head of an executive agency carrying out a program shall schedule the transfer of funds to minimize the time elapsing between transfer of funds from the United States Treasury and the issuance or redemption of checks, warrants, or payments by other means by a State.

(b) Consistent with program purposes and regulations of the Secretary and by means mutually agreed upon by the Secretary and the State, a State shall minimize the time elapsing between transfer of funds from the United States Treasury and the issuance or redemption of checks, warrants, or payments by other means for program purposes.

(c) The Secretary is authorized to issue regulations that would require a State to pay interest on funds from the time they are deposited to the

State's account until the time that they are paid out in order to redeem checks or warrants, or make payments by other means for program purposes. Such interest shall be at the rate specified from time to time by the Secretary pursuant to 31 U.S.C. 323 relating to Treasury tax and loan accounts.

(d) If a State disburses its own funds for program purposes in accordance with Federal law, regulation, or Federal-State agreement, the State shall be entitled to interest at the rate specified pursuant to 31 U.S.C. 323 from the time the State's funds are paid out to redeem checks or warrants, or make payments by other means until the Federal funds are deposited to the State's bank account. Such interest shall be paid out of the Intergovernmental Interest Fund established by Section 6309(a) of this title.

(e) If a State collects and holds refunds of grant funds, such refunds shall be distributed to the Federal Government on a timely basis or used to offset related Federal program funds owed to the State. Further, interest earned on such refunds shall be considered when setting overall interest obligations between the State and the Federal Government as required by this Act.

(f) In cases where the Federal Government makes payment on behalf of a recipient organization, the principles of this Act apply.

(g) A State may not be required by a law or regulation of the United States to deposit grant money received by it in a separate bank account. However, a State shall account for grant money made available to the State as United States Government grant money in the accounts of the State. The head of the State agency concerned shall make periodic authenticated reports to the head of the appropriate Federal executive agency on the status and the application of the money, the liabilities and obligations on hand, and other information required by the head of the executive agency. Records related to the grant received by the State shall be made available to the head of the executive agency and the Comptroller General for auditing, as prescribed in the Single Audit Act of 1984.

(h) The Secretary shall prescribe the methods of payment of interest between the Federal Government and the States, including provisions for offsetting amounts owed by the respective parties. These methods of payment shall provide for comparable treatment in the manner, technique and timing for both the States and the Federal Government.

(i) Periodically, the various Inspectors General will conduct audits, and the Comptroller General of the United States shall perform oversight evaluations. Periodic audits by the States will be conducted within the scope of work performed under the Single Audit Act.

(j) Consistent with Federal program purposes and regulations of the Director of the Office of Management and Budget, the head of a Federal executive agency carrying out a program shall execute grant awards on a timely basis to assure the availability of funds to accomplish transfers in compliance with Section 6503(a).

(k) In assessing charges to be paid by a State into the Intergovernmental Interest Fund, the Secretary shall consider costs incurred by the State in determining the amount due.

Section 5. The analysis of item 6503 of Chapter 65 of Title 31, United States Code, is amended to read as follows:

"6503. Intergovernmental Financing."

Section 6. (a) Chapter 65 of Title 31, United States Code, is amended by adding at the end thereof the following new section:

"6509. Intergovernmental Interest Fund."

(a) There is established in the Treasury of the United States a fund known as the Intergovernmental Interest Fund (hereinafter, "The Fund").

(b) The Fund shall include amounts received as payment of interest under Section 6503(c) of this title, and such sums as may be necessary to pay interest pursuant to Section 6503(d).

(c) Monies in the Fund shall be available without fiscal year limitation.

(d) The Secretary is authorized to credit such portions of the Fund as are in excess of the amount necessary to pay claims to a Treasury miscellaneous receipts account or other accounts established by the Secretary.

(e) Where interest is earned by a State on a program where only the Secretary of the Treasury is authorized to invest funds, the interest earned shall be credited to the appropriate trust fund, not to the Intergovernmental Interest Fund.

Section 7. The analysis of Chapter 65 of Title 31, United States Code, is amended by adding at the end thereof the following:

"6509. Intergovernmental Interest Fund"

Section 8. The provisions of this Act shall apply to all Federal programs and shall supercede the provisions of existing Federal laws or regulations.

Section 9. This Act is effective upon enactment. All States and Federal agencies shall be in compliance with this Act two years subsequent to the date of enactment.

November 1, 1985

DEPARTMENT OF THE TREASURY
FISCAL SERVICE

31 CFR PART 205

PAYMENTS BETWEEN THE FEDERAL GOVERNMENT AND RECIPIENT ORGANIZATIONS

AGENCY: Financial Management Service, Fiscal Service, Treasury

ACTION: Notice of Proposed Rulemaking

SUMMARY: The Fiscal Service is issuing this Notice of Proposed Rulemaking (NPRM) to implement a new funding option for Federal programs and to require payment of interest during the time Federal funds reside in a bank account.

This new "Checks Issued-Interest Remitted" technique is developed in response to statutes in some states that require that the funds reside in a state bank account prior to the issuance of payments.

This part also provides for the remittance of interest by the Federal Government to the States for the time that a state's funds are advanced for Federal programs in accordance with Federal law, regulation or Federal/State agreement. Certain provisions concerning the disallowance of costs are also included.

DATE: Comments on this proposed rule must be received in writing no later than _____.

ADDRESS: Send written comments to: Director, Funds Flow Division, Financial Management Service, Department of the Treasury, Treasury Annex No. 1, Room 802-PB, Washington, DC 20226.

CONTACT: For further information contact:

SUPPLEMENTARY INFORMATION:

Due to concerns lodged by the States regarding the delay of drawdown technique, which delays the drawdown of Federal funds until checks are estimated to clear, a Joint State/Federal Cash Management Reform Task Force, made up of State and Federal representatives, was established in 1983 to consider other cash management alternatives.

The Task Force developed a Memorandum of Understanding (MOU) that was agreed to in 1983. The MOU includes the following seventeen intergovernmental cash management policies:

1. There shall be a set of Government-wide cash management policies and practices that govern all exchanges of funds between Federal and State Governments.

2. Intergovernmental cash management practices should be such that neither the Federal nor State Government benefit financially or suffer financially as a result of the transfer of cash in support of Federal assistance programs.

3. It is understood that the Federal Government is entitled to earnings on cash provided by the Federal Government to a State government prior to the time such cash is needed to redeem a warrant, a check, or payment by other means. It is also understood that a State government is entitled to earnings on cash advanced by such State government to redeem a warrant, a check, or payment by other means, prior to reimbursement by the Federal Government on programs for which Federal payment is required.

4. The Federal Government shall make grant allocations and awards in such a manner and in such amounts to assure that funds are adequate to meet State cash disbursement issuance requirements.

5. States shall bill based on actual cash disbursement needs or a close approximation of expected cash disbursement needs (plus the allowance for depreciation, amortization, and overhead costs, as approved in accordance with OMB Circular A-87).

6. Due to the variety of constitutional, statutory, and administrative restrictions existing among the 50 states, several techniques for transferring cash between Federal agencies and State governments shall be made available for selection by each state. These techniques are:

   a. Checks paid letter of credit.

   b. Estimated checks cleared letter of credit (Delay of Draw).

   c. Checks issued letter of credit with interest paid or credited (using, for example, the Separate Bank Account or Day of Disbursement method).

7. States selecting the checks issued letter of credit with interest paid or credited option shall:

   - Draw down Federal funds as close as possible to the time of issuance of warrants, checks, or payments by other means.

   - Pay or credit the U.S. Treasury interest paid on the balance of Federal cash in banks/State treasuries based on the Federal funds rate; the specific rate and method to be determined.

8. Since the checks issued letter of credit with interest paid or credited option is new, there should first be a pilot test in three or four States in order to resolve any initial procedural or operational matters that may arise.

9. The Federal Government is willing to work with the States and state organizations to consider other financing systems or methods proposed by the States as long-range or future alternatives.

10. The Federal Government shall pay to or credit the appropriate State Treasury interest on the balance of state cash advanced on Federal programs based on the Federal funds rate; the specific method and rate to be determined.

11. Whenever feasible, each state and the concerned Federal agencies shall implement a single cash management technique for all Federal programs in which the State is participating.

12. Federal agencies and each State government will move as quickly as possible to adopt the technique(s) chosen by each state.

13. All transfers of funds between the States and the Federal Government shall be accomplished by wire transfer to ensure quick delivery of funds.

14. Where Federal statutes require reimbursement, the Federal Government shall revise regulations or administrative procedures to ensure that cash is transferred as closely as possible to the time that states make disbursements.

15. States will apply sound businesslike practices when disbursing Federal funds to secondary recipients and contractors, and not disburse or handle such cash at a faster rate or in a different manner than it handles its own cash.

16. For Supplemental Security Income State supplement payments, the same cash management principles shall be followed, except the State will be considered the disbursing agent and the Federal Government the payee.

17. Each State will designate a specific State official(s) (name and title) with the statutory or administrative authority to coordinate all state agencies to review, approve, and/or enter into an agreement with the U.S. Government for the purpose of implementing these cash management policies.

The MOU also contained an agreement to pilot in several States a new funding technique called "Checks issued-interest remitted". This technique allows states to time the draw of Federal funds to satisfy the requirements of the constitution or statutes of some states that funds be on deposit prior to the preparation of a check, warrant, or other payment.

In order to maintain equity in intergovernmental cash management, the Federal Government will pay interest when a State disburses its own funds for program purposes because Federal funds arrive subsequent to the State's need to redeem checks or warrants, or make payments by other means.

It is intended that the regulations will apply to all recipients. However, at this time the Federal Government will implement the provisions of this regulation that apply to the payment and collection of interest with state recipients only. Nothing in this regulation precludes the collection of interest from non-state recipient organizations due the Federal Government under any other regulations or statutes.

SPECIAL ANALYSIS:

The Financial Management Service has determined that this proposal is not a major rule for purposes of E.O.12291. Therefore, no regulatory impact analysis is required.

It has been certified that the rulemaking proposed herein will not have a significant economic impact on a substantial number of small entities. Accordingly, a Regulatory Flexibility Act analysis is not required.

List of Subjects in 31 CFR Part 205

Banks, Banking.

Fiscal Assistant Secretary

Date

For the reasons set out in the preamble, it is proposed to add a new Part 205 to 31 CFR, Chapter II, to read as follows:

Part 205 - Payments Between the Federal Government and Recipient Organizations

Accordingly, 31 CFR Part 205 is amended as follows:

Section

205.1 Purpose
205.2 Scope of regulations
205.3 Definitions
205.4 General regulations
205.5 Responsibilities of Federal program agencies
205.6 Responsibilities of recipient organizations
205.7 Compliance
205.8 Administrative costs
205.9 Implementing instructions

Authority: 5 U.S.C. 301; Sec. 203, 82 STAT. 1101 (42 U.S.C. 4213).

§ 205.1 Purpose

This part prescribes the regulations governing monetary transactions between the Federal Government and recipient organizations for financing operations under all Federal programs.

§ 205.2 Scope of regulations

(a) The regulations in this part apply to all exchanges of funds between the Federal Government and all recipient organizations carrying out Federal programs whether by grant or other forms of assistance agreements.

(b) Payments on contracts are subject to the provisions of the Federal Acquisition Regulations regarding contract financing which appear at 48 CFR 1 and the provisions of the Armed Forces Procurement Regulations regarding defense contracting which appear at 32 CFR 163.

§ 205.3 Definitions

For the purpose of this Part:

(a) Recipient organization means an organization outside the Federal Government (including any state and local government, educational institution, international organization, any other public and private organization or fiscal agent or institution acting on its behalf) receiving payments under any Federal program.

(b) Primary recipient organization means a recipient organization receiving payments directly from the Federal Government and any organization, such as a fiscal agent, acting on its behalf.

(c) Secondary recipient organization means a recipient organization receiving payments from a primary recipient organization.

(d) State means a State of the United States, the District of Columbia, a territory or possession of the United States, and an agency, instrumentality, or fiscal agent of a State but does not mean a local government of a State.

(e) Check means a draft, warrant, or payment by other means.

(f) Monetary transactions shall include all program payments and interest payments.

(g) Direct Treasury check means the method whereby payment is made directly to a recipient organization by Treasury check authorized by the responsible officer of the Federal program agency.

(h) In accordance with Federal law, regulations or Federal/State agreement means a recipient makes a payment under an ongoing Federal program notwithstanding the absence of a Federal appropriation.

(i) Letter of credit means a commitment, certified by an authorized official of a Federal program agency, specifying a dollar limit available to a designated payee. A period of time of availability may also be specified.

(j) Drawdown means the process of requesting and receiving Federal funds.

(k) Checks paid technique means the procedure whereby the drawdown is delayed until the checks issued for program disbursements are presented to the recipient organization's bank for payment.

(l) Delay of drawdown technique means the procedures where by the drawdown is spread out over a number of days so that daily deposits will roughly coincide with the pattern in which checks have historically been presented to the bank for payment.

(m) Checks issued-interest remitted technique means the method of drawing down funds such that Federal cash is on hand as close as possible to the day the cash is needed by the recipient for the issuance of warrants, checks, or payments by other means. Interest is remitted as provided by Sections 205.4 (e) and 205.4 (f).

(n) Interest means the interest to be charged at the rate specified from time to time by the Secretary pursuant to 31 USC 323 relating to Treasury tax and loan accounts.

§ 205.4 General regulations

(a) Payments to a recipient organization shall be limited to the minimum amounts needed and shall be timed to be in accord only with the actual, immediate cash requirements of the recipient organization in carrying out the purpose of the program or project. The timing and amount of payments shall be in accordance with the funding technique elected by the recipient organization. Recipients shall use either the checks paid, delay of drawdown, checks issued-interest remitted, or other Treasury approved technique in timing the drawdown of Federal funds.

(b) If a Federal program agency has, or expects to have, a continuing relationship with a recipient organization for at least one year, involving annual payments aggregating at least $120,000, the Federal program agency shall use the letter-of-credit method or a Treasury approved transfer method.

(c) When annual payments to a recipient organization aggregate less than $120,000 or there is not a continuing relationship for at least one year, the payments shall be made by the direct Treasury check method or a Treasury approved transfer method.

(d) Payments made by primary recipient organizations to secondary recipient organizations shall conform substantially to the same standards of timing and amount as apply to payments by Federal program agencies to primary recipient organizations. No interest obligation pertaining to the Federal Government shall be computed or paid on balances held by secondary recipients.

(e) Unless prohibited by Federal statute, State recipients shall be required to remit interest for the time Federal funds are on hand prior to being used to redeem checks or warrants, or make payments by other means for program purposes. Where used, compliance with delay of drawdown procedures will preclude payment of interest to the Treasury.

(f) When authorized by Federal statute, the Federal Government shall remit interest when the State uses its funds prior to the receipt of Federal funds to redeem checks or warrants, or make payments by other means in accordance with Federal law, regulation or Federal/State agreement.

(g) In cases where the Federal Government makes payment on behalf of a recipient organization, for example, the Supplemental Security Income program, the principles of this regulation apply. The State's remittance is to be timed to coincide with the clearance time of Federal checks or payments by other means.

(h) When a State collects and holds refunds of Federal grant funds such amounts shall be remitted to the Federal Government on a timely basis or offset against related Federal program funds. Interest if applicable on such funds shall be calculated from the first day of the month subsequent to the month in which the State collected the funds.

§ 205.5 Responsibilities of Federal program agencies

The responsibilities of Federal program agencies are:

(a) Amend or establish procedures to fund approved Federal programs and projects under methods agreed to by the Federal agency and the recipient.

(b) Promulgate internal policy designed to schedule the transfer of funds to minimize the time elapsing between the transfer of funds from the United States Treasury and the issuance or redemption of checks, warrants, or payments by other means by a recipient organization.

(c) Make grant allocations and awards for program purposes in such a manner and amounts to assure that Federal funds can be drawn timely to meet primary recipient cash requirements in carrying out Federal programs.

(d) Expedite the processing of supplemental awards and the resolution of disallowances and deferrals so as to minimize the cash flow burden on recipients and the payment of Federal interest to the States.

§ 205.6 Responsibilities of recipient organizations

The responsibilities of a recipient organization are:

(a) Draw only immediate cash requirements under mutually agreed methods for carrying out approved programs or projects.

(b) Apply sound businesslike practices when disbursing Federal funds to secondary recipients and contractors, and not disburse or handle such cash at a faster rate or in a different manner than it handles its own cash.

(c) Maintain appropriate documentation to support cash management practices.

(d) Promulgate internal policies to ensure compliance with these regulations.

§ 205.7 Compliance

(a) The Single Audit Procedures of OMB Circular A-128 shall be used to assure compliance with the provisions of this Part.

(b) To ensure compliance by Executive Agencies, the various Inspectors General are encouraged to conduct audits and the Comptroller General is encouraged to perform periodic oversight evaluations.

(c) When no Treasury approved funding technique has been selected by a recipient, such recipients may be assessed estimated interest where authorized by law for the time Federal funds are on hand prior to being used to redeem checks or warrants, or make payments by any other means for program purposes.

§ 205.8 Administrative costs

(a) Unless prohibited by Federal statute, the primary recipient shall be reimbursed for the administrative costs of procedures used to implement and maintain the elected technique through indirect cost in accordance with applicable cost principles.

(b) As an option to the above procedure where authorized by law, Treasury will allow States to submit properly documented and reasonable costs of procedures used to implement and maintain the selected technique as offsets to interest owed to the Intergovernmental Interest Fund.

§ 205.9 Implementing instructions

The Commissioner, Financial Management Service, will issue implementing instructions in Volume I of the Treasury Financial Manual for the regulations established by this Part.

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OMB Circular A-102

TO THE HEADS OF EXECUTIVE DEPARTMENTS AND ESTABLISHMENTS

SUBJECT: Uniform Administrative Requirements for Grants and Cooperative Agreements to State and Local Governments

1. Purpose. This circular establishes consistency and uniformity among Federal agencies in the management of grants and cooperative agreements with State, local, and federally recognized Indian tribal governments.

2. Authority. This circular is issued under authority of the Budget and Accounting Act of 1921, as amended, the Budget and Accounting Procedures Act of 1950, as amended, and Reorganization Plan No. 2 of 1970 and Executive Order No. 11541. Also included in the circular are standards to ensure consistent implementation of Sections 202, 203, and 204 of the Intergovernmental Cooperation Act of 1968, the Office of Federal Procurement Policy Act Amendments of 1983, and the Federal Grant and Cooperative Agreement Act of 1977.

3. Background. This revision builds upon agency experience in implementing the original Circular A-102. It updates certain provisions, provides further standard guidance to Federal agencies, and establishes common regulatory terms and conditions. The revised circular will replace a number of varying requirements now found in agency regulations and in handbooks and manuals on the same subject.

4. Coverage. All Federal agencies administering programs that involve grants and cooperative agreements with State, local and Indian tribal governments shall follow the policies in this circular and issue common regulation grants administration regulations (common regulation). If the enabling legislation for a specific grant program prescribes policies or requirements that differ from those in the circular, the provisions of the enabling legislation shall govern.

5. Exceptions. The Office of Management and Budget may grant exceptions from the requirements of this circular when permissible under existing law. However, in the interest of uniformity and consistency, exceptions will be permitted only in exceptional circumstances.

6. Pre-Award Policies.

a. Use of grants or cooperative agreements. The Federal Grant and Cooperative Agreement Act of 1977 (31 U.S.C. 6301) governs the use of grants, contracts and cooperative agreements. A grant or cooperative agreement will be used only when the principal purpose of a transaction is to accomplish a public purpose of

support or stimulation authorized by Federal statute. Contracts shall be used when the principal purpose is acquisition of property or services for the direct benefit or use of the Federal Government. The statutory criterion for choosing between grants and cooperative agreements is that for the latter, "substantial involvement is anticipated between the executive agency and the recipient during performance of the contemplated activity."

b. Advance Public Notice and Priority Setting.

(1) Federal agencies shall provide the public with an advance notice in the Federal Register, or by other appropriate means, of intended funding priorities for discretionary assistance programs. These priorities shall be approved by the head of the department or agency.

(2) Whenever time permits, agencies shall provide the public an opportunity to comment on intended funding priorities.

(3) All discretionary grant awards shall be reviewed for consistency with agency priorities by a policy level official.

c. Standard Forms for Applying for Federal Assistance

(1) Agencies shall use the forms prescribed in section __.10 of the common regulation for all programs except for those that require no application.

(a) Preapplication for Federal Assistance. The Preapplication for Federal Assistance is used to: (1) establish communication between the agency and the applicant, (2) determine the applicant's eligibility, (3) determine how well the project can compete wih similar applications from others, and (4) eliminate any proposals that have little or no chance for Federal funding before applicants incur significant costs in preparing detailed applications. Preapplication forms shall be used for all construction, land acquisition and land development projects or programs when the need for Federal funding exceeds $100,000. It may be used for other programs, if desired. In addition, agencies may establish procedures allowing state and local government applicants to submit a preapplication if they so desire, when there are no mandatory requirements for preapplication

(b) Application for Federal Assistance (Nonconstruction Programs). The Application for Federal Assistance (Nonconstruction Programs) form shall be used for all programs, except those where the major purpose is construction, land acquisition, or land development or where the application is for a single-purpose and one-time award of less than $10,000 that does not require an environmental impact statement, or the relocation of persons, businesses, or farms.

(c) Application for Federal Assistance (Construction Programs). The Application for Federal Assistance (Construction Programs) form will be used for all grants where the major purpose of the program involves construction, land acquisition, or land development.

(2) Requests by grantees for changes, continuations, and supplements to approved grants will be submitted on the same form as the original application. For these purposes, only the amended pages of the forms will be required.

(3) Agencies may specify how and whether budgets should be separately shown by functions or activities within the program or project.

(4) When additional information is needed to comply with legislative requirements or to meet specific program needs, Federal agencies shall obtain OMB clearance in accordance with the Paperwork Reduction Act clearance requirements of 5 CFR Part 1320, "Controlling Paperwork Burdens on the Public."

(5) Additional assurances shall not be added to those contained in the forms unless specifically required by law.

(6) Agencies have the option of shading out any line item on any form that is unnecessary for decisionmaking purposes or for meeting the requirements of other circulars or laws except for the Standard Form 424 facesheet. This form shall not be modified. If an item is not applicable, write or overprint "NA" in the space provided for each item.

(7) Federal grantor agencies are authorized to reproduce these forms. The Standard Form 424 can be obtained from the General Services Administration.

d. Debarment and Suspension. Federal agencies shall not award assistance to applicants that are debarred or suspended, or are otherwise excluded from or ineligible for participation in Federal assistance programs under Executive Order 00000. Agencies shall establish procedures for the effective use of the Consolidated List of Debarred, Suspended, Voluntarily Excluded and Ineligible Assistance Participants to assure that they do not award assistance to listed parties in violation of the Executive Order. Agencies shall also establish procedures to provide access to the list to their recipients and subrecipients (including contractors) at any tier, to assure that they do not make awards in violation of the Executive Order.

e. Adjustments to Awards.

(1) Agencies should make awards on an annual basis, unless awards for other periods are dictated by program requirements or funding limitations. Ordinarily awards should be made at least ten days prior to the beginning of the grant period.

(2) Agencies shall notify recipients immediately of any anticipated adjustments in program funding levels. This notice shall be provided as early as possible in the funding period, and before recipient funds have been expended. Reductions in funding shall apply only to periods after notice is provided.

Whenever an agency adjusts the amount of an award, it shall also make an appropriate adjustment to the amount of any required matching or cost sharing.

(3) When a multi-year project is funded in increments, agencies shall deobligate any amount in excess of $2,500 that has not yet been obligated by the grantee when making an award for the next period.

f. Special Conditions or Restrictions. Agencies may impose special conditions or restrictions on awards of Federal financial assistance to "high risk" applicants/recipients in accordance with section __.12 of the common regulation.

g. Waiver of "Single" State Agency Requirements.

(1) Requests to agencies from the Governors, or other duly constituted State authorities, for waiver of "single" State agency requirements in accordance with section 204 of the Intergovernmental Cooperation Act of 1968 shall be given expeditious handling and, whenever possible, an affirmative response shall be made to such requests.

(2) When it is necessary to refuse a request for waiver of "single" State agency requirements under section 204, the Federal grantor agency handling such a request shall advise the Office of Management and Budget prior to informing the State that the request cannot be granted. The agency will indicate to OMB the reasons for the denial of the request.

(3) Legislative proposals embracing grant-in-aid programs shall avoid inclusion of proposals for "single" State agencies in the absence of compelling reasons to do otherwise. In addition, existing "single" State agency requirements in present grant-in-aid programs shall be reviewed and legislative proposals developed for the removal of these restrictive provisions.

h. Patent Rights. Agencies shall use the standard patent rights clause when supporting research and development in accordance with OMB Circular A-124.

7. Post-award Policies.

a. Cash Management. Methods and procedures for transferring funds shall minimize the time elapsing between the transfer and the recipient's need for the funds.

(1) Such transfers shall be made consistent with program purposes, the Intergovernmental Financing Act, and Treasury regulations.

(2) Where letters-of-credit are used to provide funds, they shall be in the same amount as the award.

b. Recipient Financial Management Systems.

(1) In making its assessment of the adequacy of an applicant's financial management system, the awarding agency shall rely on readily available sources of information such as previous audit reports to the maximum extent possible. If additional information is necessary to assure prudent management of agency funds, it shall be obtained from the applicant or from an on-site review.

(2) The terms of grants and subgrants shall not require financial reporting on the accrual basis if the recipient's accounting system is maintained on the cash basis. When accrual reporting is statutorily required, a recipient will not be required to convert its accounting system to the accrual basis but instead may develop the accrual information through an analysis of the documentation on hand.

c. Program Income

(1) Agencies should encourage recipients to generate program income to help defray program costs. However, recipients shall not use grant-acquired equipment or services to compete unfairly with the private sector.

(2) Program income shall be deducted from total program costs as specified in the common regulation at __.25(g)(1) unless agency regulations state otherwise. Authorization for recipients to follow the other alternatives in __.25(g)(2) and (3) shall be granted sparingly.

d. Site Visits and Technical Assistance. Agencies shall conduct site visits only as warranted by program or project needs. Technical assistance site visits shall be provided only in response to requests from recipients.

8. After-the-Grant Policies.

a. Closeout.

Federal agencies shall notify a recipient in writing before the end of the award of reports that will be due, the dates by which they must be received, and where they must be submitted. Copies of any required forms and instructions for their completion shall be included with this notification.

b. Annual Reconciliation of Continuing Assistance Awards.

Federal agencies shall reconcile continuing awards annually and evaluate program performance and financial reports. Items to be reviewed include:

(1) A comparison of the recipient's annual work plan to its progress reports and project outputs,

(2) The Financial Status Report (SF 269),

(3) Request(s) for payment,

(4) Compliance with any matching, level of effort or maintenance of effort requirement, and

(5) A review of federally owned property for which the recipient is accountable.

Federal agencies shall close out a continuing agreement only after the end of the last funded continuation agreement.

9. Entitlements (Reserved)

Note: Clarifying Procedures Relating to Disputed Claims, Deferrals and Disallowances - It is recommended that the Circular and Common Rulemaking include specific language that will give states an option to accept or reject a reduction in future funding due to a disputed claim, deferral or disallowance, except where the Federal Code expressly requires that such a reduction be made. Further, that if the disputed claim, deferral or disallowance is upheld upon review, the state is then obligated to return the funds and to pay interest for the period for which the funds were held.

10. Policy Review (Sunset). The circular will have a policy review (three years from date signed).

11. Effective Date. The circular is effective (60 days from date signed).

12. Inquiries. Further information concerning this circular may be obtained from:

Financial Management Division
New Executive Office Building, Room 10215
Office of Management and Budget
Washington, D.C. 20503

Telephone: (202) 395-3050

Director

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